Policies for Full Employment

Edited by:
Duncan Cameron
and
Andrew Sharpe

Canadian Council on Social Development

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Canadian Council on Social Development
Ottawa/Montreal

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Canadian Cataloguing in Publication Data

Main entry under title:
Policies for full employment

Bibliography: p
ISBN 0-88810-381-6 (bound)
ISBN 0-88810-377-8 (pbk.)

1. Canada – Full employment policies. I. Cameron, Duncan, 1944- . II. Sharpe, Andrew III. Canadian Council on Social Development.

HD5706.P64 1988 339.5'0971 C88-090036-9

Printed and bound in Canada by Love Printing Services Ltd.
Cover art: Barbara Szoka

Published by:
Canadian Council on Social Development
55 Parkdale Ave.
P.O. Box 3505, Station C
Ottawa, Ontario K1Y 4G1

To the memory of

Professor Jack Weldon

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FOREWORD

Employment means more than economic security. For most Canadians it is a prerequisite to individual independence and social status.

And yet, when inflationary pressures in the seventies convinced governments to kick the stuffing out of the employment market in order to make our economy lean and mean, the cost was not fairly shared. We did not all "tighten our belts," as the common cliché suggested.

Instead, we watched as the most vulnerable of businesses, and the most vulnerable of people, were relegated to the economic sidelines. There were more than a few. Perhaps 25 per cent of the labour force paid the price of this adjustment: the young and inexperienced; older workers with obsolete skills; unlucky workers whose jobs had become automated; and those with the more traditional disadvantages: lack of education, disability, or discriminatory treatment.

Canadians felt for the unfortunate. They wanted governments to do something, even though they didn't feel that governments could create jobs directly. And political parties responded. They all promised jobs. And they all watched and waited as a revigorated economy entered a sustained period of growth. They watched as new jobs were created at a normal rate, enough to absorb the growth of the population seeking jobs, but not enough to provide reasonable or secure opportunities for that large group of unfortunate unemployed people. Then a peculiar thing happened; increasingly, it was suggested that with all the temporary support from unemployment insurance, food banks, and soup kitchens, maybe these people had lost their incentive to work. Governments, after all, couldn't be all things to all people.

And so the debate continues. Does society have an obligation to provide citizens with the opportunity to make a decent living? If so, by what means? This book explores these questions; in the meantime, the unemployed and underemployed wait. But with little optimism.

We should point out, as we always do with books of this nature, that the opinions expressed are those of the authors and editors, and do not represent the

views of the Canadian Council on Social Development, nor of the Ottawa-Carleton Social Planning Council.

A special thanks to all involved, especially Andrew Sharpe and Duncan Cameron, who contributed a great deal of their time and talent.

Terrance Hunsley
Executive Director
CCSD

ACKNOWLEDGEMENTS

This book originated as a project of the Income and Employment Committee of the Social Planning Council of Ottawa-Carleton. Committee members organized a Symposium on Policies for Full Employment in the Fall of 1985, where all but two of the selections in this book were initially presented and subsequently revised for publication. In addition to the editors and Jean-Pierre Voyer, committee members include Lin Buckland, Catherine Casserly, Bill Gillies, Ron Melchers, Arthur Milner and My Dos Santos. Ellen Adelberg and Cynthia Farquharson also assisted, as did Valerie Lavergne of the Social Planning Council. Special thanks go to Jim Davidson, the committee staff person who did much of the work in organizing the symposium, and to Frank Martin, Executive Director of the Social Planning Council, for his encouragement and support.

Our thanks to the Canadian Council on Social Development, and its Executive Director, Terrance Hunsley, for agreeing to undertake the publication of this work. CCSD communications branch staff provided editorial assistance, and managed the manuscript through the various stages of production to publication. Bill McIntosh, a former CCSD staff member, translated the article by Diane Bellemare and Lise Poulin Simon.

Ginette Rozon, Louise Clément, and Phuong Chi Hoang of the research secretariat at the Faculty of Social Sciences, University of Ottawa, provided word processing assistance. The Department of Political Science of the University of Ottawa gave material support.

In addition to the contributors to this volume, participants in the Symposium program included Caroline Andrew, University of Ottawa; Marion Dewar, former mayor of Ottawa and now Member of Parliament for Hamilton Mountain; Sym Gill, Canadian Auto Workers; John McCallum, University of Quebec at Montreal; Don McGillivray, Southam News Services; Lionel Orlikow, former deputy minister of labour, Government of Manitoba; Arthur J.R. Smith, former chief executive officer, Canadian Labour Market and Productivity Centre; Joseph Verbruggen, Canadian Employment and Immigration Commission;

Peter Warrian, Peter Warrian and Associates; and, Jack Weldon, McGill University.

Support in organizing the Symposium was provided by the Mayor's Office and the Economic Development Branch of the City of Ottawa, the National Capital Commission, the Ottawa Citizen, Andrés Wines, the National Union of Provincial Government Employees, the Canadian Centre for Policy Alternatives, the Ottawa-Carleton Board of Trade, the Ottawa and District Labour Council and the Central Volunteer Bureau.

On February 26, 1987, our friend and colleague Jack Weldon passed away in Montreal at the age of 65. We remember him for his commitment to social justice, his inspiration as a teacher and his intellectual integrity. As an historian of economic thought, he recognized that economic life is subject to change for the better when common people realize their own capacity to act. In dedicating this volume to his memory, we honour his unflagging determination that Canada be a better country.

Jack believed that we had to banish forever the scourge of unemployment. And he thought that this could be done, and he worked to make it happen. Jack never quit acting for the common good.

INTRODUCTION

Almost without realizing it, Canada has abandoned a political commitment by Parliament in 1945 to consider full employment the basic objective of economic policy and a fundamental criterion of economic success.[1] Indeed, many of today's economic and political decision-makers believe an economy with well over one million unemployed Candians is a more or less normal state of affairs, something about which little can be done. In this book, we question this assessment. In our view, joblessness is not necessarily a permanent feature of Canadian society. Nor is this simply a matter of preferring an optimistic outlook to a pessimistic one. High levels of unemployment surely have something to do with political choices. This collection shows that appropriate policies could have a significant impact in reducing unemployment.

All the available evidence indicates that unemployment is of great concern to Canadians. In presentations to Royal commissions, and other public statements, many groups and individuals have attested to what the opinion survey data show — that Canadians think unemployment is the most important problem facing Canada. According to the November, 1986 Gallup Poll, fully 61 per cent of Canadians believed priority should be given to reducing unemployment rather than balancing the budget. Joblessness has been identified as "the most important problem facing Canadians" since the beginning of 1983, and was a concern for the majority of Canadians in both 1984 and 1985, according to Gallup. Unfortunately, there has not been adequate public debate in Canada about the many concrete policy alternatives that could reduce unemployment. The question of what can be done *now* to reduce unemployment needs to be addressed, urgently. That is the purpose of this collection.

If reducing unemployment is a widely shared concern, why has so little been done in Canada to promote policies for full employment? Part of the answer is that economic conditions in Canada have weakened the social consensus that traditionally supported full employment. Business groups, which have never accepted the overriding importance of full employment, were able to gain allies in government, and press their more immediate concerns for profit restoration as the basis for new investment and ultimately job creation.[2] The inflationary crisis of the 1970s, culminating in 'stagflation', the world recession of 1981-82, and persistent joblessness despite economic growth, have all contributed to discouragement among many of the labour and social groups that have traditionally pushed for full employment.[3]

An earlier period of relative prosperity encouraged the view that government policy makers, acting on the basis of specialized knowledge, could promote job creation for all people seeking work through the proper manipulation of fiscal and monetary levers. More recently, we have discovered that these very same levers can be used to throw people out of work and create depression-like unemployment conditions. We conclude from this experience not that government policies are ineffective in assuring employment growth, but rather that they have been framed by other concerns. Fighting inflation, reducing deficits and social restraint have replaced job creation as economic priorities, because government agendas have been dominated by groups favouring these policies.

It is interesting to note that the struggle against inflation and in favour of fiscal prudence has often been waged using the language of job creation. Calls for deficit reduction and social spending restraint are accompanied by pleas for tax breaks to create jobs. This shows the enduring appeal of employment policy and leaves the door open for the re-establishment of full employment, defined as jobs for all, as the principal goal of economic policy.

But it would be a mistake for Canadian groups that advocate a full employment strategy to simply rely once again on the technical knowledge of government policy-makers to assure employment growth. The retreat from full employment shows the need for political mobilization behind concrete measures for job creation. It also underlines the importance of refuting the conventional thinking of business groups, which are never shy about presenting their own self-interest as the national interest.

Our concern, then, is that the political commitment to *full* employment be renewed. If this is to happen, it must be shown that full employment is indeed an essential and feasible goal for society, that policy options are available to reduce and ultimately eliminate unemployment, and that evidence exists that should convince people who, for whatever reason, have abandoned the concept of full employment, that they have been mistaken to do so. This type of analysis may well be a prior condition to any effective political action. However, we also believe that the erosion of the commitment to full

employment has gone so far that we must show, as a starting point, that high levels of unemployment are not inevitable in Canada.

For this reason, the authors who contributed to this volume were asked to focus on immediate measures to reduce unemployment. Though a good case can be made that a fundamental social and economic transformation of Canadian society is desirable, the point of this collection is not to propose such a transformation. Rather, the scope is more modest. These papers suggest that unemployment is something over which we have considerable control. We can, as citizens, through our institutions, take decisions which increase the number of jobs available. This does not require major political change. Indeed, for a significant political transformation to occur, it may well be necessary to achieve full employment first.

This view of the continued importance of full employment as a contemporary political goal is controversial. Though political parties continue to emphasize job creation, and no one seriously doubts the politiçal attractiveness of reducing unemployment, there is little unanimity in Canada about the future of work and employment. One scenario suggests that full employment has become an out-moded concept in a post-technological society, where it will not be necessary for people to waste their time on meaningless work. Abundant material wealth will free up time for many citizens to enjoy the benefits such a society can provide, without having to toil unneccessarily.[4]

This scenario assumes that the production and distribution of wealth are separate activities. Making the additional assumption that political and social mechanisms can be developed to facilitate the transfer of wealth from those who control its production to those who would enjoy the benefits of enhanced productivity appears improbable and unrealistic in the absence of fundamental political change. In fact this view is unlikely to figure as an item on Canada's political agenda as long as salaries and wages remain at the centre of material existence for the overwhelming majority of Candian workers and would-be workers.

A more significant view is that full employment is not an affordable policy at present. Full employment, defined as a job for everyone seeking employment, is said to exact unacceptable costs by causing rapid inflation. As well, we are told that a full employment policy would constitute a guaranteed existence for Canadian workers, leading to distortions in the job market and reduced discipline in the labour force. Eventually, Canada would be unable to compete in international markets, while inflation and increased rigidities in the labour market would erode Canadians' standard of living.[5] These arguments, which are very much a part of the Canadian political agenda, are debated in this book.

The popularity of these neo-conservative views in business circles, their adoption by the Macdonald Commission, and their influence on the policy advice received by government are partly a reflection of the prescriptions put forth by the new conservatives for increasing employment and dealing with

people who remain without paid work. They believe that wage flexibility, and the operation of a market unfettered by government intervention and regulation, provide the surest basis for employment creation without inflation. A guaranteed annual income could replace various costly social programs with an all-inclusive plan that would be more efficient and less expensive than the present welfare state.

But neo-conservatives often obscure the fact that market solutions to unemployment impose steep social costs. Given a guaranteed income, then left to the mercy of market forces, the poor and disadvantaged would become even less able to create a decent existence. The strategy of "leaving it to the market" threatens labour unions, communities, universal social programs, local institutions, and other democratic forces in society. By imposing on society an even greater role for the market, it is entirely possible that powerful corporations will simply be given more power. Most important, such reliance on the presumed natural laws of supply and demand implies that people have little say in their own economic destiny, that little can be done to change social circumstances, and therefore that little *should* be attempted politically.

Such a view of our social and political existence is based on a poor understanding of history, and equally poor theory. The market may well figure in economic history as a central institution, but other more democratic institutions have been created to mitigate the most unacceptable features of its performance. All market activity in Canada is in some sense subsidized by government. Such diverse programs as education, road-building, postal service, health care and police services are used and taken for granted by market participants, but do not enter into calculations of supply and demand except as costs to be paid for the burden of government. When such non-market institutions promote economic growth, it is a mistake to consider that only market activity is productive. Though production of economic goods occurs mainly in institutions that respond to market forces, firms operate under dynamic historical conditions that are imperfectly represented by the static analysis of supply and demand.

Yet these unrealistic assumptions of market analysis have become socially embedded. Market economists have transformed hypotheses into beliefs. The assumption that wage flexibility allows the labour market to clear leads to the analysis that wage inflexibility explains unemployment, and the policy prescription that wage rigidities should be eliminated. Such thinking ignores historical evidence about the way in which wages are determined, treats human beings as if they were commodities for trade, and suggests that by restraining collective bargaining, doing away with social security nets, and eliminating minimum wage laws policy-makers could eliminate unemployment. While it is no doubt true that many people would be tempted to hire the unemployed if wages fell far enough, and that many unemployed would be forced to work for low wages if social security were eliminated, such one-dimensional analysis ignores the power relations that underlie the market

and the social brutality of low wages. By turning relations between individuals into simple market transactions, such thinking obscures the political character of society and its ability to frame needs, concerns and goals through non-market as well as market institutions.

It should be pointed out that chronic unemployment has been a subject of debate in academic and policy circles for many years. Most meaningful debate has focused on the historical development and structuring of the Canadian economy. It is not our intention to repeat this debate, but some elements of the discussion should be kept in sight. The impact of foreign investment on Canada's capacity to control its job creation destiny is one important theme. Against the conventional view that such investment creates additional wealth and jobs, it has been shown that foreign control impedes domestic research and development, exports, and innovation, and creates pressure on the balance of payments. Similarly, having the highest level of foreign ownership of any industrialized country influences the structure of Canada's international trade. A horrendous deficit in manufactured end products means that Canada is a net importer of goods with a high degree of labour content, essentially importing labour in spite of a perpetual labour surplus at home.[6]

Another disappointing feature of the Canadian economy is the performance of public investment. While it is generally accepted that public investment expenditures should be used to stabilize the economy, increasing at times when private investment is weak, analysis shows that public investment represents a declining share of the Gross National Expenditure. Rather than serving to expand economic activity at times when the job market is weak, public investment seems to fluctuate like private investment.[7] The nature of Canadian federalism, which provides important spending powers for provincial and some municipal governments, contributes to a structural inability to link public investment spending with job creation.

The concentration of ownership in the Canadian economy, fueled by tax provisions that encourage mergers and takeovers, is another structural barrier to job creation. Indeed, the rationalization of Canadian industry has made layoffs and job disappearance the most efficient features of the Canadian economy.[8] The tax system itself is biased against labour. By providing write-offs for new machinery and equipment, it directly subsidizes capital investment, discriminates against the hiring of workers, and encourages the replacement of human jobs with machines.[9]

There is no shortage of suggestions that would transform the structural conditions of job creation. Leo Panitch of York University has suggested that much as we have created school boards to ensure that education be universally available for children, we should establish locally elected labour boards with a mandate to meet full employment goals.[10] Phillip Resnick of the University of British Columbia has argued that traditional full employment means the perpetuation of a social order that revolves around mindless

consumerism and routine, mind-numbing work. He suggests that the capacity for human self-expression reflected in interesting work must somehow be associated with a new social definition of employment. Paid work and satisfying human endeavours have grown in such divergent ways, he says, that only a re-thinking by society of the nature of employment can begin to touch upon the realities of joblessness.[11]

Mainstream opinion has also embraced employment strategies. Clarence Barber presented an important statement on unemployment to his fellow members of the Macdonald Commission, only to have it set aside.[12] Ruben Bellan of the University of Manitoba has argued that the federal government has the capacity to eliminate the social waste associated with unemployment.[13] We are pleased to note that public debate on unemployment has been widened with the publication of the Dryden report on youth unemployment in Ontario, and the release of a Newfoundland task force report on unemployment. Dryden has no difficulty in defining full employment as jobs for everyone who is looking for work. Though he does believe that unemployment must be understood as a permanent problem before anything can be done about it, he calls upon the Ontario government to adopt a full employment policy.

Thus, while the Forget report on unemployment insurance can be seen as one more attempt to encourage market solutions for social questions, there remains serious opposition to the neo-conservative agenda. A Parliamentary committee examining the Forget recommendations reached an all-party agreement that they should be shelved. Perhaps a better recognition that market forces have wrought unacceptable social consequences, and that neo-conservative prescriptions are no more intelligent today than in the Depression years of the 1930s, when they were widely practiced, would constitute a wise beginning to a more thoughtful public debate.

The frameworks proposed in this book differ on the extent to which unemployment can be reduced, and on the effectiveness of various policy options. Because of the scope of the problem, important elements of the debate around full employment could not be fully treated. Closer examination of fiscal, trade, and industrial policy would certainly be desirable, and disagreements over policy remain. But the contributors to this volume share a concern about certain overall unemployment trends in Canada:

- The emergence of part-time rather than full-time employment as the major component of new job creation is remarkable. From 1976 to 1986, part-time jobs increased by 76 per cent, while full-time work increased by only 17 per cent. More disturbingly, while only 11 per cent of part-time workers wanted full-time jobs in 1975, some 30 per cent — about 500,000 Canadians — were involuntary part-time workers in 1985.

- The regional distribution of new jobs is uneven. From 1981 to 1986, no net employment creation occurred in British Columbia, and Alberta saw a one per cent decrease in jobs. Of the 137,000 new jobs created from

January, 1986 to January, 1987, an astounding 132,000, or 96 per cent, were in Ontario.

- Overtime remains a common practice, despite widespread unemployment and opposition by government and the Canadian Labour Congress. It has been calculated that about ten per cent of Canadian workers receive overtime pay, to work an average of eight overtime hours per week.[14] Business remains opposed to any change in this practice, even though it has important implications for employment policy.

- An important, common theme that emerges in these pages is that unemployment has simply not been taken seriously enough in this country. Too often, analysis of the problem has obscured the issue rather than encourage public discussion. Public participation in the debate over the future of Canada's jobless is crucial for organizations like the Canadian Council on Social Development and the Ottawa-Carleton Social Planning Council.

In the paper that opens this collection, the Social Planning Council of Ottawa-Carleton puts forward arguments about the nature, costs and causes of unemployment. It examines the economic conditions that surround unemployment in Canada, concluding that unemployment reached crisis proportions because of restrictive government policies introduced across the western world. The paper demonstrates that most joblessness can be explained, not by new entrants to the labour market failing to find jobs, or by people leaving jobs, but by the elimination of existing jobs. This analysis differs from the findings of the Macdonald Commission, which singled out demographic changes and labour market rigidities as the main explanations for unemployment.

Stephen McBride surveys recent writings about employment policy and the future of work. He judges full employment to be a feasible, practical political goal. He finds that the rejection of Keynesian policy alternatives may be premature since some state intervention has been a part of all successful employment policies. When they have been applied as a part of a political commitment to full employment, national policy measures seem to be effective in maintaining high levels of employment. Indeed, for McBride, the best historical evidence suggests that there is no need to accept that mass unemployment is part of an inevitable trend for advanced industrialized countries.

The unemployment crisis is a world-wide problem that has persisted despite a limited economic recovery. In Section II, Diane Bellemare and Lise Poulin Simon describe how some countries maintained full employment throughout the world recession. While economic growth is commonly seen as a prerequisite to job creation, Bellemare and Poulin Simon show that the relationship is better understood as flowing in the opposite direction, that employment growth is crucial to income growth. They demonstrate that the income growth foregone through unemployment far exceeds the cost of any job creation program, thus refuting the argument that Canada cannot afford

full employment. Austria, Norway, Sweden and West Germany have found their own solutions to the job creation challenge, and while Canada need not take other countries' experience as a model to be replicated here, it is clear that their success can be duplicated if a similar commitment to full employment is made. Such a commitment must be flexible, to meet different regional conditions in Canada.

To a remarkable degree, the full employment challenge is a community concern. It is in our neighbourhoods that we have a unique identity, that we stand out as more than simply employed or unemployed Canadians as measured by Statistics Canada. In Section III, David Ross looks at the prospects for community economic development, and Penina Coopersmith examines the potential for job creation through the renewal of municipal infrastructure.

Ross points out that the weakening of the welfare state and the loss of traditional jobs has contributed to the growth of alternative economic enterprises. He describes the form that some of these local economic initiatives have taken, and shows what makes them different from conventional businesses. While current government policies do not provide significant assistance to this not-for-profit sector, Ross argues that the ingenuity demonstrated by various cooperative enterprises holds out promise for the future. While community development enterprises are unlikely to be a major solution for the type of employment crisis that Canada has experienced, their very existence demonstrates a will to find alternative means of living together. Furthermore, an improved government policy framework could substantially increase their job creation potential .

Coopersmith presents a program developed for the Federation of Canadian Municipalities, showing that jobs could be created through a collaborative effort by the three levels of government to repair and replace Canada's decaying municipal infrastructure. Many of the urban services that we take for granted are deteriorating badly, and the longer we wait to bring them up to standard, the more expensive the job will be. Moreover, the construction costs would yield significant employment benefits. When assistance for municipal infrastructure is measured against other public spending programs, its job creation potential makes it an attractive alternative.

Central government policies set the overall framework within which other job creation programs become more feasible or more difficult. Throughout the recent inflationary period, the role of monetary policy as administered by the Bank of Canada has been growing in importance. Indeed, since the abandonment of fixed exchange rates by most industrial nations in the early 1970s, much of the weight of economic stabilization has been carried by monetary policy. The rapid movement of interest-rate-sensitive funds from country to country has led national authorities to doubt their ability to insulate domestic money markets from international influences. Given the advanced degree of Canadian monetary integration with the United States, external constraints on

domestic monetary policy are widely believed to limit the role of the Bank of Canada in employment creation.

This conventional view is examined and found wanting by Michael McCracken. In Section IV, he argues that Canada has not fully exploited its floating exchange rate to bring down domestic interest rates. His model shows that lower interest rates would have a positive, if small impact on employment, and that the fear of increased inflation is largely unfounded. He proposes that monetary authorities reduce real interest rates from levels that are unacceptable for job creation purposes to more normal rates. This would mean re-establishing an historic relationship between market rates and inflation of about three per cent, rather than the much higher levels of recent years.

A preoccupation with inflation has been the justification for restrictive policies in Canada and elsewhere. It has been held that inflation is a greater danger to Canadian society than unemployment, and that full employment policies would rekindle inflationary fires. Tim Hazledine offers a solution to the belief that society is forced to make unacceptable choices between higher unemployment or renewed inflation, arguing that price controls can be an acceptable anti-inflation policy precisely because they allow society to continue pursuing employment goals. His analysis suggests that critics of price controls have failed to look seriously at what such a program entails. It does not necessarily mean less efficiency or less equity to control prices rather than to allow them to be set by large firms. In fact, his analysis shows that price controls may well transform firms that are presently price-makers into price-takers, so that many of the benefits of market competition would be recovered.

According to Hazledine, any attempt to stimulate the economy in the absence of price controls will simply be dissipated through price increases by major corporations. Though it may unsettle many observers, his analysis merits close attention, if only because it is one of the few attempts to seriously explore how price controls would work and what impact they might have.

Section V looks at the labour market, to see what can be done to reduce unemployment through work-time reduction or wage subsidization. Frank Reid examines the feasibility of legislative intervention to shorten the work week, voluntary work reduction schemes, and proposals for short-time compensation to workers who would otherwise be laid off. Given that rather small changes in hours worked across the Canadian economy are accompanied by large shifts in the unemployment rate, Reid argues that society would be better off if work could be shared across a broader base in times of cyclical decline, rather than imposing the burden of unemployment on specific individuals. If it is believed that little can be done to stimulate the economy directly, employment sharing is an obvious alternative to the more traditional definition of full employment as a full-time job at a full wage.

Arthur Donner and Mel Kliman examine the controversial view that wage subsidization could be used to reduce unemployment. Some analysts believe that current schemes such as unemployment insurance essentially subsidize individuals to remain idle, and argue that it would be much better for society and the individuals to subsidize firms to engage them in productive activity. Critics cast this proposal as a form of workfare, and a regression from the rights gained under the welfare state.

Wage subsidies may in fact force unemployed individuals to accept unsatisfactory employment against their will, simply to retain access to a form of social assistance. While their future employment opportunities may not be improved, their rights under a social wage would be diminished. In addition, such a program could simply encourage employers to replace regular employees with wage-subsidized employees. But despite these serious objections, the authors argue that wage subsidization may have a role as one element of a larger program to reduce unemployment, and that it merits close attention in any event because of its popularity in government circles.

Because of the great importance of the partisan political debate on employment policy, the three major parties were invited to present their views on alternative job creation programs. The trade critic for the Liberal Party, Lloyd Axworthy, concludes that Canada cannot avoid certain choices in industrial policy if current unemployment problems are to be resolved, and if jobs are to be found for new entrants to the labour market. He foresees the need for greater cooperation between various levels of government to deal with the special problems of hard-core unemployment in various regions of Canada and among particular groups of Canadians. Above all, he warns that full employment goals will require great effort to overturn the prevailing mood that government programs are unable to deal with unemployment.

Jim Hawkes, speaking from his experience as Progressive Conservative Chairperson of the House of Commons committee on employment policy, suggests that Parliamentary reform will lead to new forms of policy-making by government. In future, House committees will be more directly involved in generating new ideas and programs. Though he thinks it would be a mistake to look for a grand policy design from his party, Hawkes contends that his party will pay more attention to the practical difficulties of increasing employment than the previous government. He notes that immigration policy is an important factor in the search for full employment, since new immigrants bring capital and entrepreneurial skills to bear on job creation.

The Deputy House Leader of the New Democrats, Lorne Nystrom, is concerned that government policy initiatives like the movement toward free trade with the United States will have a negative impact on employment. He notes that Crown corporations have been used to create jobs, and suggests that privatization will lead to job loss. He sees the tradition of cooperative enterprise as an important aspect of Canadian heritage, and a positive force for employment. The New Democrat task force on employment found that

Canadians in all regions support an increase in local authority over government policies and are suspicious of central control, whether it is based in provincial capitals or in Ottawa. Mr. Nystrom believes a commitment to ensuring that people make a living at home is being eliminated in favour of policies that will force Canadians to give up their regional identities in order to find employment in central Canada.

This book presents commentary and discussion on what we think should be the first item on Canada's political agenda: policies for full employment. We believe the goal of full employment is unassailable on both economic and social grounds, and that it is achievable as well. But for full employment to become a reality will require a recognition of the true causes of unemployment, and a commitment to social and economic policies in which job creation is the central objective.

In order for the debate on full employment to lead to political action, it will be necessary to broaden the base of discussion and increase the number of participants. It is only by making their views known and their voices heard that citizens of a democracy are empowered to force political change.

Full employment is not just an economic variable to be manipulated in the name of anti-inflation policy, any more than unemployment is simply a statistical measure of the number of Canadians looking for work. In both cases, it is necessary to go beyond conventional discourse and standard categories if we are to understand and deal with the challenge we face. Until the monopoly on economic wisdom is broken, so that citizens meeting and discussing policy among themselves have the same opportunity as economic experts to contribute to public debate, even broad popular support for full employment will likely lead nowhere.

Duncan Cameron

NOTES

1. The commitment to full employment was somewhat less than unanimous. See Cy Gonick, *The Great Economic Debate* (Toronto: James Lorimer and Co., 1987), p. 87.
2. Ibid.
3. Definitions of full employment are linked to the analysis of unemployment. Social and labour groups have no trouble seeing full employment as a condition where there are enough full-time jobs for everyone looking for work. More recently, it has been redefined to mean a level of unemployment consistent with price stability. For a discussion of these definitions see O. Ashenfelter, "What is a Full Employment Goal in the

1980s?", *Labour Market Development Task Force Technical Studies Series*, July 1981.

4. A clear statement of this position is put forth by Philip Resnick, "The Mirage of Full Employment", *New Internationalist*, December 1986.
5. This is the analysis of the Macdonald Commission, in *Royal Commission on the Economic Union and Development Prospects for Canada: Volume One* (Ottawa: Minister of Supply and Services, 1985), pp. 50-57.
6. See Glen Williams, *Not For Export* (Toronto: McClelland and Stewart, 1983).
7. Duncan Cameron, "Wage Earners, the Liberals and the Canadian Economy", *Our Generation*, Spring 1983.
8. See *Possibles*, Winter 1987. The theme of this issue is "Un emploi pour tous?".
9. On this subject, see Gregory Baum and Duncan Cameron, *Ethics and Economics* (Toronto: James Lorimer and Co., 1984).
10. Leo Panitch, "A Socialist Alternative to Unemployment", *Canadian Dimension*, June-July 1986.
11. Resnick, "The Mirage of Full Employment", op. cit..
12. This statement is reproduced in Clarence Barber, "Jobs, Jobs: Specific Proposals", *Policy Options*, April 1986.
13. Ruben C. Bellan, *The Unnecessary Evil* (Toronto: McClelland and Stewart, 1986).
14. Frank Reid, "Overtime Work in Canada", A study for the International Labour Office, Geneva, November 1985.

An Overview of Unemployment

In this overview section, two contributions examine the impact of unemployment. The first looks at unemployment in Canada; the second compares the retreat from full employment thinking with evidence showing that full employment can be successful.

One way of underlining the need for full employment policies is to examine the impact of unemployment on Canadian society. The article by Sharpe, Voyer and Cameron presents the nature, costs and causes of unemployment, and shows that official figures mask its extent. Important phenomena, such as the discouraged worker and the prevalence of part-time workers who would prefer to be working full-time, are hidden from view. New trends like the increasing duration of unemployment are easily missed. Reported variations in unemployment rates may not reveal who bears the burden of joblessness. The social costs of unemployment and the cost to society in terms of foregone income are not well appreciated. In order to present a more complete view of unemployment, all these elements are described and analyzed.

This first article also refutes the argument that increased unemployment is in some sense voluntary. The forceful return of classical views of unemployment has important implications for labour market policy; these explanations and policy options are examined and found wanting.

In order to grasp the meaning of the unemployment crisis, it is necessary to understand that expert debate is unlikely to resolve it. This paper concludes that Canadians should not be discouraged by the lack of consensus that characterizes informed debate among economists over the causes of unemployment. Indeed, the contrasting views should encourage concerned Canadians to add their own voices to public discussion. In a democracy, technical analysis can never replace the weight of public opinion.

In the second article, Stephen McBride contrasts two views of employment policy. The "Post Employment Society" is shown to be inferior to the "Full Employment Society". McBride concludes that comparative historical analysis of employment policies demonstrates the importance of political choices in determining the level of unemployment.

I

UNEMPLOYMENT: ITS NATURE, COSTS AND CAUSES

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Canada's unemployment rate averaged 9.6 per cent in 1986 (see Table I-1). In absolute terms, this meant that 1,286,000 individuals were officially unemployed. While the unemployment rate was down from a monthly peak of 12.8 per cent in December, 1982, and an annual peak of 11.9 per cent in 1983, it was still much higher than post-war levels. From the start of the Second World War until 1981 the unemployment rate had never been above 8.3 per cent. The unemployment rate rose progressively in the seventies, from an average 4.4 per cent in the 1966-70 period to 6.1 per cent from 1971 to 1975 and 7.7 per cent from 1976 to 1981. The 1981-82 recession produced a drastic increase in the unemployment rate. From 1982 to 1985 the unemployment rate was above 10 per cent every year, well above historical levels.

By international standards, the Canadian unemployment rate is high. Data for 1986 show that Canada ranked seventh highest among the 16 largest OECD countries — behind Spain, Belgium, the Netherlands, Great Britain, France and Italy. In sharp contrast to this high Canadian unemployment rate, Norway recorded 1.9 per cent unemployment, Japan 2.8 per cent, Sweden 2.7 per cent and Austria 3.1 per cent.[1] Moreover, while the Canadian unemployment rate has traditionally followed American patterns, it has been significantly above the American rate since 1981. In 1984, the Canadian rate averaged almost four percentage points higher than the U.S. rate — 11.3 per

Table I-1

Unemployment in Canada, 1966-1986

Year	Number of Unemployed (thousands)	Unemployment Rate (per cent)
1966	251	3.4
1967	296	3.8
1968	358	4.5
1969	362	4.4
1970	476	5.7
1971	535	6.2
1972	553	6.2
1973	515	5.5
1974	514	5.3
1975	690	6.9
1976	726	7.1
1977	849	8.1
1978	908	8.3
1979	836	7.4
1980	865	7.5
1981	898	7.5
1982	1314	11.0
1983	1448	11.9
1984	1399	11.3
1985	1328	10.5
1986	1236	9.6

Source: Statistics Canada. *Historical Labour Force Statistics*, Cat. 71-201, February 1987.

cent versus 7.5 per cent. By 1986, the difference had been reduced to 2.6 points — 9.6 per cent versus 7.0 per cent.

Unemployment is expected to remain high for the rest of the 1980s, assuming no major policy changes. The Department of Finance, in the June, 1987 Tax Reform Statement, forecast that the unemployment rate would only fall to 8.9 per cent by the fourth quarter of 1988 and average 8.0 per cent over the 1989-92 period. Other projections show the unemployment rate remaining near or above nine per cent into the early nineties (see Table I-2).

Table I-2

Unemployment Rate Forecasts

	1988	1989	1990	1991	1992
Data Resources Incorporated	8.8	9.1	9.0	8.6	8.4
University of Toronto	9.6	9.4	9.2	9.0	8.8
Informetrica	8.9	8.6	9.1	8.2	7.7
Conference Board	9.0	8.5	9.1	9.0	8.5
Wharton Econometrics	8.7	8.5	10.1	10.3	10.2
Economic Council (Base Case)	8.5	8.2	8.3	8.2	7.1
Department of Finance (Fourth Quarter)	8.9	8.0*	→	→	→

* Average 1989-92

Sources: Data Resources Incorporated - *Canadian Review*, Fall 1987, Toronto; University of Toronto, Policy and Economic Analysis Program - *National Projections Through 2001: Base Scenario and Alternatives*, January 1987; Informetrica - *The Canadian Economy to 2005, Assumptions and Summary*, Post-Workshop I-87, August 1987; Conference Board - *Quarterly Canadian Forecast*, Fall 1987; Wharton Econometrics - *Canadian Long-Term Economic Forecast and Analysis*, October 1987; Economic Council - *Reaching Outward - 24th Annual Review*, September 1987; Department of Finance - Tax Reform 1987, *Economic & Fiscal Outlook*, June, 1987.

Hidden Forms of Unemployment

The official unemployment rate does not measure the true degree of unemployment and underemployment in the economy, for two main reasons. First, the employed in the labour force survey are defined as those at work in the reference week, even if they only work one hour. No distinction is made between part-time and full-time workers. Part-time work does not constitute a form of underemployment when it reflects a voluntary choice by the worker, but it does when it is involuntary.[2] The proportion of part-time workers who would prefer full-time employment rose from 11.0 per cent in 1975 to 18.5 per cent in 1981, and to a peak of 30.1 per cent in 1984. By 1986, despite the recovery, 28.4 per cent of part-time workers would still have preferred full-time work if it had been available. Moreover, the growth of part-time employment has been substantially greater than that of full-time employment — 71.0 per cent versus 12.2 per cent — between 1975 and 1986, with part-time jobs rising from 10.6 to 15.6 per cent of total employment. From 1981 to 1986, full-time employment grew only 3.2 per cent, from

Table I-3

Supplementary Measures of Unemployment in Canada, 1976-86

	Official Unemployment Rate	R_1	R_2	R_3	R_4	R_6	R_7	R_8	R_9
1976	7.1	2.4	5.6	—	7.1	7.5	7.9	7.9	9.7
1977	8.1	2.8	6.3	7.9	8.0	8.8	9.0	9.2	9.6
1978	8.3	3.1	6.7	8.1	8.3	9.1	9.3	9.6	10.3
1979	7.4	2.6	6.0	7.2	7.4	8.2	8.4	8.7	10.2
1980	7.5	2.5	6.0	7.2	7.4	8.4	8.5	8.9	9.6
1981	7.5	2.6	6.2	7.3	7.5	8.5	8.6	9.0	9.8
1982	11.0	4.5	9.2	10.8	10.9	12.7	12.5	13.3	11.6
1983	11.9	5.8	10.0	11.7	11.8	13.9	13.3	14.5	13.0
1984	11.3	5.2	9.8	11.1	11.2	13.4	12.5	14.0	13.0
1985	10.5	4.8	9.1	10.3	10.4	12.5	11.6	13.1	12.8
1986	9.6	4.1	8.4	9.5	9.5	11.6	10.6	12.1	10.8

Note: R1 - Persons unemployed 14 or more weeks as a percentage of the labour force.

R2 - Unemployment rate of persons heading families with children under 16 years of age.

R3 - Unemployment rate excluding full-time students.

R4 - Unemployment rate including full-time members of Canadian Armed Forces.

R6 - Unemployment rate of full-time labour force.

R7 - Unemployment rate including persons not in the labour force who sought work in the past six months, but have stopped looking for labour-market-related reasons.

R8 - Underutilization rate based on hours worked and hours "offered."

R9 - Unemployment rate of part-time labour force.

Source: Statistics Canada. *The Labour Force*, Cat. 71-001, February 1987.

9,519,000 to 9,824,000, while part-time employment rose 21.7 per cent, from 1,487,000 to 1,810,000.

The official definition of the unemployed also excludes discouraged workers who have stopped actively looking for work and left the labour force because they believe no work is available, and individuals outside the labour force who do not seek employment because of limited opportunities. This discouragement is manifested either by absolute drops in the labour participation rate, or slower-than-expected growth in participation. From 1981 to 1982, the aggregate participation rate fell from 64.8 per cent to 64.1 per cent, and by 1986 had only risen to 65.7 per cent, still below projected trends. During the recession, the discouraged-worker effect was particularly dramatic among young people and older workers, particularly men. Labour force participation among young adults fell from 67.7 per cent in 1981 to 65.8 per cent in 1982, as young people returned to school or prolonged their stay in school, and had only increased to 68.6 per cent in 1986. Similarly, the participation rate for males over 55 fell from 45.6 per cent in 1981 to 40.6 per cent in 1986, as many older workers were involuntarily forced into retirement.

Since 1979, Statistics Canada (in the March Labour Force Survey) has been asking persons outside the labour force who want and are available for work why they are not seeking it. The number of respondents who believe no work is available rose from 83,000 in March, 1979 to 197,000 in March, 1983, before declining to 105,000 in March, 1986. If these discouraged workers had been considered part of the labour force in 1983, the unemployment rate would have been two percentage points higher, 13.9 per cent rather than 11.9 per cent.

Another indicator of discouragement is the number of people who are outside the labour force because they lost their job or were laid off. Many of these workers would still be in the labour force if their job still existed. The number of individuals in this category rose slowly from 476,000 in 1976 to 573,000 in 1981, jumped to 766,000 in 1982 and 835,000 in 1983, then declined slightly to 775,000 by 1986. It is clear that the recession led to a significant increase in the number of individuals who left the labour force because of job loss. By 1986 this number was still above the pre-recession level.

Statistics Canada recognizes the limitations of the official unemployment rate, and provides supplementary data which attempt to take account of hidden unemployment (see Table I-3). For example, when the definition of unemployment includes people outside the labour force who sought work in the past six months but have stopped looking for reasons related to the labour market, the 1983 unemployment rate becomes 13.3 per cent, compared to the official rate of 11.9 per cent. When it is based on hours worked and hours "offered", the peak unemployment rate jumps to 14.5 per cent in 1983 because of increased part-time and short-time employment during the recession.[3] Even by 1986, the unemployment rate based on hours worked and hours offered was still 12.1 per cent, well above the 9.6 per cent official rate.

Table I-4

Unemployment by Age and Sex in Canada, 1975-1986

	Both Sexes			
	15-24	**25-44**	**45+**	**Total**
1975	12.0	5.4	4.4	6.9
1976	12.7	5.7	4.2	7.1
1977	14.4	6.3	4.9	8.1
1978	14.5	6.7	5.1	8.3
1979	12.9	6.0	4.5	7.4
1980	13.2	5.9	4.5	7.5
1981	13.2	6.2	4.4	7.5
1982	18.8	9.4	6.7	11.0
1983	19.9	10.4	7.4	11.9
1984	17.9	10.2	7.5	11.3
1985	16.5	9.5	7.2	10.5
1986	15.2	8.7	6.6	9.6
	Male			
	15-24	**25-44**	**45+**	**Total**
1975	12.5	4.0	3.9	6.2
1976	13.2	4.6	3.7	6.3
1977	14.9	5.2	4.4	7.3
1978	15.0	5.5	4.7	7.5
1979	13.2	4.9	4.0	6.6
1980	13.7	5.2	4.0	6.9
1981	14.1	5.3	4.1	7.0
1982	21.1	9.1	6.6	11.1
1983	22.4	10.3	7.4	12.1
1984	19.4	9.9	7.3	11.2
1985	18.2	8.9	7.1	10.3
1986	16.5	8.3	6.3	9.4
	Female			
	15-24	**25-44**	**45+**	**Total**
1975	11.4	7.1	5.4	8.1
1976	12.1	7.6	5.0	8.4
1977	13.8	8.2	5.9	9.4
1978	13.8	8.7	5.9	9.6
1979	12.7	7.8	5.4	8.8
1980	12.6	7.0	5.5	8.4
1981	12.3	7.5	4.9	8.3
1982	16.1	9.8	6.9	10.9
1983	17.0	10.5	7.6	11.6
1984	16.2	10.6	7.8	11.4
1985	14.6	10.3	7.5	10.7
1986	13.8	9.3	7.7	9.9

Source: Statistics Canada. *Historical Labour Force Statistics*, Cat. 71-201, February 1987.

The Incidence of Unemployment

The incidence of unemployment and changes in unemployment over time both vary among groups. Table I-4 shows that unemployment is much higher for young adults (15-24 years) than prime age adults (25-44 years), and higher for prime age adults than older adults (45 years and over). In 1986, the unemployment rate for young adults was 15.2 per cent, compared to 8.7 per cent for prime age adults and 6.6 per cent for older adults.

It is particularly interesting to note the relative changes in unemployment rates by age group. In 1975, unemployment was 2.22 times as prevalent among youth as it was in the 25-44 age group, and 2.73 times as prevalent as among older adults. The 1981 differentials (2.13 and 3.00) were similar. In 1982, however, unemployment rose 51.6 per cent for prime age adults and 52.3 per cent for older adults, compared to 42.4 per cent for youth. More importantly, between 1982 and 1986 unemployment declined much more rapidly for youth than it did for the other two age groups. By 1986, youth unemployment was only 1.75 times the rate for prime age adults, and 2.30

Table I-5

Unemployment Rates by Industry in Canada, 1975, 1981-86
All Classes of Workers

	1975	1981	1982	1983	1984	1985	1986
Agriculture	2.8	4.5	6.4	7.2	6.9	7.1	6.6
Fishing and Trapping	-	11.1	10.4	13.7	14.5	17.1	14.4
Forestry	19.4	19.9	28.7	25.3	24.9	25.4	25.2
Mines, Quarries & Oil Wells	5.6	6.1	12.9	13.7	10.9	8.9	10.6
Manufacturing	7.4	7.9	13.4	13.0	11.0	10.1	8.8
Construction	11.8	12.7	20.5	23.9	22.7	20.0	17.6
Transport, Communication and Utilities	4.9	5.1	7.5	8.3	7.9	7.2	6.9
Trade	5.6	6.5	9.6	10.5	9.9	8.9	8.5
Finance, Insurance and Real Estate	2.9	3.9	5.3	6.0	5.8	6.2	4.7
Community, Business and Personal Services	5.4	6.8	9.2	10.2	10.1	9.6	8.8
Public Administration	4.2	5.4	7.0	7.8	8.9	8.3	7.7
All Industries	6.9	7.5	11.0	11.9	11.3	10.5	9.6

Sources: Statistics Canada. *Labour Force Annual Averages, 1975-83*, Cat. 71-529, February 1984, and *The Labour Force*, Cat 71-001, December 1984, 1985 and 1986.

Table I-6

Unemployment by Occupation in Canada, 1975, 1981-83, 1986

	1975	1981	1982	1983	1986
All Occupations	6.9	7.5	11.0	11.9	9.6
Managerial, Administrative	2.1	2.2	3.7	4.1	4.4
Natural Sciences	2.8	3.2	6.4	7.8	6.3
Social Sciences	3.6	4.8	6.2	6.3	6.3
Religion	—	—	—	—	1.1
Teaching	3.4	3.3	4.2	4.7	4.5
Medicine and Health	3.1	2.8	3.8	3.9	3.5
Artistic and Recreational	5.9	8.5	10.0	11.8	10.2
Clerical	5.5	6.3	9.0	9.9	8.0
Sales	4.3	5.2	7.9	8.6	7.4
Service	7.4	9.7	12.6	13.9	12.2
Agriculture	3.7	5.5	7.8	9.4	8.5
Fishing, Hunting and Trapping	—	11.5	10.6	13.8	13.4
Forestry - Logging	21.3	23.4	31.9	28.3	29.6
Mining and Quarrying	8.9	9.3	18.6	17.9	14.1
Processing	9.6	9.7	16.2	15.3	11.7
Machining	7.1	7.5	16.6	19.3	10.5
Product Fabricating, Assembling and Repairing	7.0	7.9	13.1	12.6	9.0
Construction Trades	10.8	12.1	19.0	22.1	16.9
Transport Equipment Operation	6.5	8.0	12.3	12.7	10.5
Materials Handling	10.9	11.6	18.1	18.0	13.7
Other Crafts and Equipment Operating	4.7	5.5	7.4	8.4	7.0

Note: Data for all classes of workers

Source: Statistics Canada. *Labour Force Annual Averages, 1975-83*, Cat. 71-529, February 1984, and *The Labour Force*, Cat. 71-001, December 1986.

times the rate for older adults. These differentials may continue to drop in the future, because of the low growth rate of the 15-24 age group. Unfortunately, as the incidence of unemployment continues to shift towards workers over 25 years of age, the group that experiences higher unemployment will be the same baby boomers who are having trouble finding work today.[4]

Table I-4 also shows that the male unemployment rate has been below the female rate for every year since 1975 except 1982 and 1983, when men experienced a much larger increase than women due to the recession — 4.1 versus 2.6 percentage points in 1982. The increase in the unemployment rate in 1982 was also more pronounced for prime age males than for prime age females — 3.8 percentage points versus 2.3.

Table I-5 shows the rate of unemployment for all classes of workers by industry. In 1981, forestry workers experienced the highest rate of unemployment, at 19.9 per cent, followed by construction workers (12.7 per cent) and workers in fishing and trapping (11.1 per cent). By contrast, unemployment was lowest for workers in finance, insurance and real estate (3.9 per cent), and in agriculture (4.5 per cent). Between 1981 and 1986, the largest increases in unemployment occurred in goods-producing industries such as mines, quarries and oil wells, construction, and forestry.

Unemployment also varies greatly among occupations. While white collar occupations had significantly lower unemployment rates in 1986 than blue collar occupations, Table I-6 shows that the increase in unemployment rates during the recession was often greater for white collar workers. Unemployment in managerial and administrative jobs doubled from 2.2 per cent to 4.4 per cent from 1981 to 1984, a higher rate of increase than for traditional blue collar jobs. For the first time ever, many white collar workers are experiencing unemployment, although their joblessness rates are still well below those of blue collar workers.

The Duration of Unemployment

Table I-7 shows that the average duration of unemployment, after being relatively stable from 1976 to 1981, rose from 15.1 weeks in 1981 to 21.8 weeks in 1983, and had only declined slightly to 20.8 weeks by 1986. The percentage of the unemployed whose unemployment exceeded 14 weeks increased from 33.9 per cent in 1981 to 49.0 per cent in 1983 before falling to 43.0 per cent in 1986.

Another measure of the duration of unemployment is the proportion of the unemployed who spent 14 weeks or more looking for work. This figure rose from 32.2 per cent in 1981 to 47.0 per cent in 1983, and fell only to 41.5 per cent by 1986. As well, the proportion of the unemployed who had been out of work for over a year rose to 23.0 per cent in 1983 and fell to only 20.4 per cent in 1986, after remaining relatively stable between 1975 and 1981 (17.8 per cent and 16.4 per cent). Unpublished Statistics Canada data[5] reveal that long-term unemployment is four to 10 times higher among workers in primary and construction occupations than among high-level managerial and administrative workers.

The average duration of unemployment increases with age, as older workers experience significantly more difficulty finding employment than their younger colleagues. In 1986, older female workers remained unemployed for

Table I-7

Average Duration of Unemployment in Canada by Age and Sex, 1976, 1981-86 (in weeks)

	Both Sexes			
	15-24	**25-44**	**45+**	**Total**
1976	12.2	14.7	17.3	13.9
1981	13.0	15.9	19.3	15.1
1982	15.4	18.0	20.4	17.3
1983	18.4	23.1	26.7	21.8
1984	16.8	23.0	27.9	21.6
1985	15.8	23.1	29.6	21.6
1986	14.5	21.4	29.0	20.8
	Males			
	15-24	**25-44**	**45+**	**Total**
1976	12.2	15.1	17.8	14.1
1981	13.4	17.0	20.5	15.9
1982	15.8	18.7	21.3	17.9
1983	19.3	25.0	27.5	23.1
1984	17.2	24.8	29.4	22.9
1985	16.3	24.9	32.1	23.1
1986	15.1	22.7	31.0	21.5
	Females			
	15-24	**25-44**	**45+**	**Total**
1976	12.1	14.3	16.5	13.6
1981	12.6	14.7	17.4	14.2
1982	14.7	17.2	19.0	16.4
1983	17.1	20.5	25.2	19.9
1984	16.3	20.7	25.4	19.8
1985	15.1	21.0	25.7	19.7
1986	18.8	20.0	26.0	18.8

Source: Statistics Canada. *Labour Force Annual Averages, 1975-83*, Table 39, Cat. 71-529, February 1984, and *The Labour Force*, Cat. 71-001, December 1984, 1985 and 1986.

an average of 26.0 weeks, 7.2 weeks above the average for all unemployed women. Older male workers stayed unemployed an average of 31.0 weeks, 9.5 weeks over the average for all unemployed men. It is interesting to note that, unlike younger workers, the average duration of unemployment for older workers has not diminished during the recovery, indicating that older workers are having greater problems adapting to changing labour market conditions than younger workers.

Table I-8

Flows into Unemployment in Canada, 1975-86 (percentage of total unemployment)

	Job Losers	Job Leavers	Entrants	Re-entrants 1 year or less	Re-entrants more than 1 year
1975	39.4	27.8	5.8	18.6	8.1
1976	46.3	23.3	5.6	16.4	8.4
1977	50.5	21.1	5.7	13.9	8.8
1978	50.3	21.1	5.8	13.5	9.3
1979	48.4	20.1	6.1	15.1	10.3
1980	49.7	19.7	5.5	14.8	10.4
1981	50.1	19.0	5.3	14.9	10.6
1982	59.3	15.0	4.4	11.8	9.5
1983	59.3	13.8	4.8	10.6	11.4
1984	57.3	15.5	4.8	10.5	11.9
1985	55.6	17.2	4.4	11.1	11.8
1986	55.5	18.0	4.1	11.4	11.1

Source: Statistics Canada. *Labour Force Annual Averages, 1975-83*, Cat. 71-529, February 1984, and *The Labour Force*, Cat. 71-001, December 1984, 1985 and 1986.

Reasons for Unemployment

Table I-8 provides interesting information on the reasons for unemployment. The proportion of the unemployed who were laid off rose significantly from 39.4 per cent in 1975 to 50.5 per cent in 1977, and then from 50.1 per cent in 1981 to 59.3 per cent in 1983, before falling slightly to 55.5 per cent in 1986. Conversely, the proportion of the unemployed who left their jobs voluntarily fell from 27.8 per cent to 21.1 per cent between 1975 and 1977, and from 19.7 per cent to 13.8 per cent between 1981 and 1983, before rising to 18.0 per cent by 1986.

Additional insight into unemployment flows is contained in the Annual Work Patterns Survey.[6] While the average unemployment rate for 1985 was 10.5 per cent, 25.4 per cent of the labour force experienced unemployment at some time during the year, although only 1.9 per cent of the labour force was unemployed throughout the year. Two observations emerge from these statistics. First, unemployment in the course of a year affects a much larger proportion of the labour force than the unemployment rate would indicate. Second, few people are officially unemployed for the complete year,

indicating that most of the unemployed combine periods of employment, unemployment, and withdrawal from the labour force.

Unpublished Statistics Canada data[7] show that a considerably larger proportion of blue collar workers experience unemployment over the year than white collar workers, particularly professionals. Only 9.3 per cent of management/administration workers experienced some unemployment in 1982, compared to 22.6 per cent of clerical workers, 43.0 per cent of workers involved in material handling and 71.8 per cent of workers in forestry. The level of education also affects the distribution of unemployment. Of those with a university degree, only 14.7 per cent experienced some unemployment in 1982, compared to 23.8 per cent of those with some post-secondary education and 30.8 per cent for those with only secondary or elementary education.

The Hardship of Unemployment

The post-1981 rise in unemployment has meant increased economic hardship for many Canadians. In families with at least one unemployed person, heads of families were unemployed in 40.4 per cent of the cases in 1986, compared to 34.6 per cent in 1981 and 33.6 per cent in 1976. The share of total unemployment accounted for by heads of family units rose from 26.9 per cent in 1981 to 31.1 per cent in 1984, before falling to 30.0 per cent by 1986. The proportion of families with at least one unemployed person where no one else was employed increased from 25.6 per cent in 1981 to 29.5 per cent in 1983, and was virtually the same in 1986 (29.1 per cent). The unemployment rate for persons heading families with children under 16 jumped from 6.2 per cent in 1981 to 10.0 per cent in 1983 and was still 8.4 per cent in 1986. These statistics indicate that the recovery from the 1981-82 recession had not by 1986 reduced the economic hardship resulting from unemployment to pre-recession levels.

Regional Unemployment Trends

A particularly important characteristic of Canadian unemployment rates, which has important policy implications, is the wide regional variation. In 1986, unemployment was much higher in the four Atlantic provinces, Quebec, Alberta and British Columbia than in Ontario, Manitoba and Saskatchewan (see Table I-9). Economic recovery from the run-up in unemployment during the 1981-82 recession was notable in Ontario, Manitoba and Quebec, which by 1986 had almost reached the pre-recession unemployment rate. On the other hand, the unemployment rates in all other provinces in 1986 were still at least two points above the 1981 rates, and in the case of Alberta and British Columbia, still six points above the 1981 rate, due to the much weaker economic recovery in these two provinces.

Table I-9

Unemployment Rates by Region, 1981-86

	1981	1982	1983	1984	1985	1986
Newfoundland	13.9	16.8	18.8	20.5	21.3	20.0
Nova Scotia	10.2	13.2	13.2	13.1	13.8	13.4
P.E.I.	11.2	12.9	12.2	12.8	13.2	13.4
New Brunswick	11.5	14.0	14.8	14.9	15.2	14.4
Quebec	10.3	13.8	13.9	12.8	11.8	11.0
Ontario	6.6	9.8	10.4	9.1	8.0	7.0
Manitoba	5.9	8.5	9.4	8.3	8.1	7.7
Saskatchewan	4.7	6.2	7.4	8.0	8.1	7.7
Alberta	3.8	7.7	10.8	11.2	10.1	9.8
British Columbia	6.7	12.1	13.8	14.7	14.2	12.6

Source: Statistics Canada. *Historical Labour Force Statistics*, Cat. 71-201, February 1987.

Economic Costs of Unemployment

The standard approach to measuring the economic cost of unemployment was developed in the early 1960s by Arthur Okun, an American economist.[8] Okun estimated that each percentage point of unemployment above four per cent (the level thought to be consistent with price stability) was associated with a three per cent fall in real Gross National Product.[9] Based on this estimate, Canada's 9.6 per cent unemployment rate in 1986 resulted in lost output equivalent to 16.8 per cent of GNP!

More recently, it has been suggested that the level of unemployment associated with price stability, or the non-accelerating inflation rate of unemployment (NAIRU), has risen — the Macdonald Commission believed it ranged between 6.5 to 8.0 per cent. It has also been suggested that, for a variety of reasons, the Okun coefficient has fallen in the last decade from three to two. But, even with these more conservative estimates of NAIRU and the Okun coefficient, the lost output in 1986 would be in the range of 3.2 to 9.3 per cent of GNP, still a very large amount.

Moreover, it is well recognized that NAIRU is not full employment. Thus, the true economic costs of unemployment are much greater than 3.2 to 9.3 per cent of GNP. Even accepting conservative estimates of NAIRU and the Okun coefficient, however, 9.3 per cent of GNP represented a loss of $47 billion dollars in 1986, almost $2,000 for every man, woman and child in Canada!

Social Costs of Unemployment

There is a great deal of literature identifying the many negative effects of unemployment on the individual and society.[10] There is a direct link between poverty and unemployment, with the incidence of poverty increasing when unemployment rises. The National Council of Welfare links the rise in the proportion of Canadians living below the poverty line, from 14.7 per cent in 1981 to 17.8 per cent in 1984, to rising unemployment. Families whose heads worked 49 to 52 weeks experienced a 5.5 per cent poverty rate in 1983, those employed 40 to 48 weeks experienced a 12.4 per cent poverty rate, while those working only 20 to 29 weeks experienced a 22.4 per cent incidence of poverty.

The need for welfare is also directly proportional to the level of unemployment. A Manitoba study showed that approximately 97 per cent of the monthly change in the number of welfare recipients from 1979 to 1981 could be explained by changes in the unemployment rate.[11]

The work of Harvey Brenner in the United States has stressed the negative impact of unemployment on the social pathology of individuals. Brenner found that unemployment leads to increased stress, higher incidence of health problems, increased rates of suicide and crime, higher death rates, and loss of self-respect. A very important study by M. Jahoda concluded that the psychological impact of unemployment is as destructive today as it was in the thirties, notwithstanding the enormous social changes that have occurred since then. The unemployed also experience significant deterioration of their skills through disuse.

While all society loses becauses of unemployment, the economic and social costs are borne disproportionately by the unemployed, who in turn are concentrated disproportionately among youth, in blue-collar occupations, and among those with low skill and education levels. The tragedy of unemployment is that it is the weakest members of society who are most affected.

A further negative effect of unemployment is that it detracts from the need to humanize existing jobs. Society's energy is directed toward reducing unemployment, not improving the quality of work. Given high levels of unemployment, employers have less incentive to increase wages and fringe benefits or improve working conditions. Lower unemployment would thus be a boon, not only to the unemployed, but to all members of society.

The Causes of Unemployment

The debate over the causes of unemployment and the most appropriate policies to reduce it has not stopped since the Depression of the 1930s. But economists have yet to reach a consensus on the reasons for the recent wave of high unemployment rates in Canada. If anything, the severity of unemployment since 1982 has served to intensify the controversy.

With the development of theories explaining unemployment trends over the last several decades, an elaborate vocabulary on the nature and causes of unemployment has been built up. Unemployment is classified as structural, cyclical, frictional, classical, seasonal, involuntary, voluntary, and Keynesian. Experts refer to a natural rate of unemployment or a non-accelerating inflation rate of unemployment, or introduce the concepts of "new unemployment" and "turnover unemployment". This proliferation of terms has created confusion about the nature and the real causes of unemployment.

At the risk of over-simplification, the causes of unemployment can be classified into two major categories: cyclical causes, i.e., unemployment due to inadequate aggregate demand; and non-cyclical causes, or linked to demographic, structural, institutional or other factors.

Similarly, the present debate on the causes of unemployment can be divided into two major currents. The controversy surrounds the relative importance of the cyclical and non-cyclical components in the actual unemployment rate, and of various economic prescriptions flowing from the respective diagnoses. One side stresses the importance of cyclical causes, the involuntary nature of unemployment, and the need for government action aimed at stimulating aggregate demand. The other side stresses structural and institutional "rigidities", which require other types of government intervention. In the latter view, the adoption of expansionary economic policies is not a desirable or viable option.

It may appear simplistic to reduce the different economic schools of thought to two major currents. Yet, public debate on unemployment often reveals just such a polarization of discussions and opinions around those favouring and opposing demand stimulation.

Inadequate Aggregate Demand

Keynesian or neo-Keynesian economists believe that the major part, or at least a significant part, of the current unemployment rate is due to inadequate aggregate demand, which can be corrected by the adoption of expansionary fiscal and monetary policies. Three major reasons are given for this lack of demand:

1) The central government has relied on an increasingly restrictive monetary policy since the mid-1970s, driving interest rates to record levels in 1981 and causing the 1981-82 recession. Despite the subsequent fall in nominal rates, real interest rates have remained well above historical levels and hampered the growth of consumer, housing and investment expenditures.

2) Federal and provincial governments have adopted fiscal policies aimed at reducing their deficits. This artificial straightjacket has impeded job creation, real disposable income growth and consumer spending.

3) Federal and provincial governments have instituted restrictive wage policies that reduced the purchasing power of public sector workers, and had a negative impact on worker and consumer confidence in general.

For this school of thought, the appropriate medicine for the Canadian economy is the political will to stimulate the components of final demand. The experience of the United States, where expansionary fiscal policy lowered unemployment to the six per cent range, is often cited as evidence of the success of aggregate demand expansion.

For the Keynesians and neo-Keynesians, the rise in unemployment from 7.5 per cent in 1981 to the higher range experienced recently is explained entirely by the recession, followed by a recovery that has not been sufficient to close the new gap between employment and labour force growth. Most economists within this group also believe that a large part of the 7.5 per cent

Table I-10

Job Vacancies All Categories,* Unemployment, and Job Vacancies as a Percentage of Unemployment, Canada, 1971-1978

	Job Vacancies All Categories (thousands)	Unemployment (thousands)	Job Vacancies All Categories (as % of unemp.)
1971	37.4	535	7.0
1972	66.2	553	12.0
1973	85.8	515	16.7
1974	101.7	514	19.8
1975	63.3	690	9.2
1976	51.4	727	7.4
1977	44.4	850	5.2
1978	44.5	911	4.9

* Categories include full-time, casual, part-time, seasonal and temporary jobs.

Source: Reproduced from S.H. Ingerman, *Improving Flexibility in Canada's Labour Force*, paper presented at the National Economic Conference, Ottawa, March 22-23, 1985, and Statistics Canada, Labour Division. *Annual Report on Job Vacancies*, 1978.

unemployment that prevailed from 1979 to 1981 was due to a shortage of aggregate demand. They point out that the rise in unemployment from 5.3 per cent in 1974 to 8.3 per cent in 1978 was accompanied by a significant reduction in job vacancies as a percentage of unemployment (see Table I-10). Statistics Canada stopped gathering job vacancy data in 1978, but there is no reason to believe that this trend has been drastically reversed. These economists also point out that average capacity utilization rates were well below the pre-1974 levels between 1974 and 1981 (Table I-11).

Recent government research tends to support the view that a major part of the 7.5 per cent unemployment rate in 1981 was cyclical:

> "Inadequate growth in aggregate demand during the latter half of the 1970s and especially during the outset of the 1980s caused the cyclical component of unemployment to rise significantly."[12]

> "These findings emphasize that unemployment (pre-recession period) is basically a demand deficiency problem rather than a turnover problem."[13]

The Keynesians and neo-Keynesians do not deny that non-cyclical factors can affect unemployment. Many would concede that the floor rates of non-cyclical unemployment have risen since the beginning of the 1970s, and that micro-economic policies are a necessary supplement to macro-economic

Table I-11

Capacity Utilization Rates in Canadian Manufacturing Industries 1971-1986

Year	Annual Average of Utilization Rates	Year	Annual Average of Utilization Rates
1971	84.4	1979	87.7
1972	87.5	1980	83.0
1973	92.7	1981	80.5
1974	91.9	1982	69.5
1975	82.3	1983	72.0
1976	84.4	1984	75.8
1977	83.3	1985	77.7
1978	85.1	1986	77.0

Source: Statistics Canada, *Capacity Utilization Rates in Canadian Manufacturing*, Cat. 31-003. July 1987.

demand management policies aimed at reducing unemployment to acceptable levels. This group generally puts foward a global strategy of labour market interventions to give the labour force the adaptive skills it needs to cope with changing economic circumstances. However, such a strategy is considered futile if it is not accompanied by expansionary macro-economic policies to promote rapid employment growth.[14]

Non-Cyclical Causes

Based on a range of theoretical frameworks, the second group of economists rejects expansionary fiscal and monetary policies as the principal tool to fight unemployment. This group minimizes the importance of cyclical unemployment and places the emphasis on the non-cyclical causes of unemployment — sometimes by conviction, sometimes for strategic reasons.

For some, unemployment has very little or nothing to do with deficient aggregate demand. It is largely a voluntary phenomenon linked to demographic factors, excessive government regulation, or taxes impeding the functioning of capital and labour markets. Demand management policies are thus impotent in reducing unemployment, because they are not relevant to current circumstances.[15] This group does acknowledge that demand management policies could play a role in reducing unemployment in some situations.

For another group of economists, associated with the "new classical" school, active demand management policies are totally ineffective in reducing unemployment. Economists like Lucas, Sargent and Barro believe that fiscal and monetary policies have no effect on output and employment, even in the short run. Rational expectations on the part of economic agents render stabilization policies ineffective. In other words, individuals have an intuitive understanding, not only of economic events occurring in their own particular industry or market, but also of the way in which general monetary and fiscal policy will affect them. Efforts by governments to adjust policy in response to economic events will have no effect on their behaviour. Producers will not change their level of output, and unemployment will remain unchanged.

Finally, a third sub-group of economists refuse to consider expansionary macro-economic policies because of their effect on the budget deficit. They fear that a rising government debt/GNP ratio will significantly impair future economic growth. More important, in their view, is the possible resurgence of inflation if governments try to reduce unemployment below the non-cyclical unemployment threshold, or non-accelerating inflation rate of unemployment (NAIRU), through expansionary economic policies. This point of view has been adopted by the Macdonald Commission:

> As we Commissioners have already made clear, we accept the view that, given the present structure of the economy, demand management policies alone cannot reduce unemployment below 6.5 per cent on a sustained basis. It is for this reason that we attach such importance to

> structural initiatives which could lower the attainable floor rate of unemployment. Moreover, we think that it could be very unwise to risk our recent reduction in inflation, purchased at such great cost, by attempting to use demand management policy alone to return unemployment very rapidly to the 6.5 to 8 per cent range.[16]

But what are these non-cyclical causes of unemployment evoked by the opponents of aggregate demand stimulation? The rest of this section will briefly review some of these factors.

Frictional Unemployment

Frictional unemployment refers to the portion of unemployment caused by labour turnover, the movement of workers from one job to another. Workers who leave a job or are laid off require a certain amount of time to find another suitable job. Similarly, new labour force entrants, students, and housewives need time to find a job. This type of unemployment is often of short duration, and is not considered a serious problem. It is even considered desirable, since the time between jobs enables workers to acquire better information on existing jobs, wages, and working conditions.

At the end of the 1950s, the unemployment rate that corresponded to full employment was estimated around two per cent, believed to be the irreducible level of frictional unemployment. This estimate was based on the observation that unemployment averaged about two per cent during the Second World War and the years immediately following, when the Canadian economy was operating at full capacity.

Recently, a new school of thought has developed around the concept of "new unemployment" or "turnover unemployment". According to the proponents of this theory, unemployment which appears to be caused by inadequate aggregate demand is, in fact, frictional. If certain groups experience high rates of unemployment, it is not because they are without work for a long period of time, but because they are often without work for short periods of time. Because these workers have uninteresting work, they change jobs frequently, going from one undesirable job to another. This approach tends to downplay the burden of unemployment by suggesting that unemployment is more closely linked to frequent worker turnover than to a general shortage of jobs.

The solution to unemployment, according to this school, is to adopt manpower policies that facilitate the flow of labour market information to the unemployed, to reduce the time between jobs and improve the match between workers and jobs. In addition, income maintenance systems such as unemployment insurance, which reduce the cost of job search and encourage unemployment, should be reviewed.

Research on Canadian labour markets has found that most periods of unemployment are short, from two to three months on average.[17] However, a large

proportion of the unemployed remain without work for longer periods, and these spells of joblessness represent a large share of total unemployment. As we have noted, 43 per cent of total unemployment in 1986 was accounted for by spells of unemployment over 14 weeks. Moreover, when worker discouragement is factored in, the average duration of unemployment rises considerably, as 44 per cent of all unemployment spells end in the worker's exit from the labour force.

Thus, contrary to the beliefs of the "new unemployment" school, short, frequent jobless spells are not the major causes of high unemployment. Rather, the frequent phenomenon of long periods of unemployment suggests that an inadequate supply of acceptable jobs, not labour turnover, is at the root of the problem.

Structural Unemployment

During the late 1950s and early 1960s, the notion of structural unemployment became increasingly popular as an explanation of the persistence of unemployment above the frictional level.[18] Structural unemployment stems from a mismatch between the requirements of the available jobs and the qualifications of the unemployed. It can arise when workers are unable to adapt to rapid technological progress. It can also arise when there is a change in the sectoral composition of output, such as a relative increase in the production of services compared to goods, or when the demand for goods purchased in a given region is permanently reduced, forcing workers to move or acquire new skills.

Initiatives since the 1960s to reduce structural unemployment have included labour training and retraining programs, relocation assistance, direct job creation programs targeted at severely affected workers or regions, and wage subsidy programs.

Acceleration of technological change, particularly the development and diffusion of micro-electronics and robotics, is often cited as a major structural cause of today's high unemployment rate. It is true that the introduction of new technologies can reduce the demand for workers with outmoded skills, and that these workers may have difficulty finding new jobs in fast-growing industries requiring different skills. However, current levels of unemployment cannot be explained so easily. To quote the Macdonald Commission report:

> There is no significant evidence that the massive unemployment of the 1930s or the present day resulted from technological change. Most of those examining both periods would agree that the sharp rise in unemployment resulted from the fact that total demand for goods and services in the economy fall considerably short of the economy's ability to purchase them...

> ... Over the period for which we have reasonable data on the composition of unemployment, there is no evidence that structural unemployment caused by technological change has ever accounted for a major share of total unemployment over a large geographic area and during extended periods of time. Structural unemployment caused by technological change can be significant in smaller regions and for certain groups of workers (especially older workers), but it has not been a major contribution to the long-term pattern of national unemployment in Canada or in other comparably industrial countries.[19]

Demographic Factors

Increases in the shares of women and young people in the labour force are two demographic changes which are said to have contributed to rising unemployment rates in the 1970s.[20] There are two main channels through which these demographic changes have affected the unemployment rate. First, changes in the demographic composition of the labour force are bound to affect the overall unemployment rate, which is calculated as a weighted average of the unemployment rates of different groups based on each group's share in the labour force. Since the female and youth unemployment rates have been higher than the prime age male unemployment rate in recent years, it is argued that the increase in relative share for these two groups raised the overall unemployment rate. This shift in the composition of the labour force is estimated to have increased the unemployment rate by 0.3 percentage points over the 1960s and the 1970s.[21]

The rapid growth of the female and youth labour force is also said to increase the unemployment rate because of the limited degree of substitution between different labour force groups. According to this explanation, certain occupations have traditionally been dominated by a particular demographic group, and penetration of these occupations by other groups may be too slow to absorb the increased labour supply.

This situation occurs if characteristics linked to the production process are associated with sex or age. For instance, it is argued that young entrants in the labour market are inevitably inexperienced, and that women generally have different skills and occupational characteristics than men. If the production process is designed at any given moment to use fairly rigid mixes of skills and occupations traditionally associated with the prime age male group, youth and women will have difficulty filling the available jobs. Empirical studies have found that this structural demographic problem was present over the 1970s, and resulted in a one percentage point increase in the unemployment rate.[22]

In any case, demographic factors cannot explain the rise in the unemployment rate in the 1980s. On the contrary, labour force changes in recent years should in theory be reducing the aggregate unemployment rate. The proportion of the labour force under 25 is falling rapidly, as the baby boom

generation matures. The proportion of women in the labour force is still rising, but the female unemployment rate is now almost identical to the male rate, so this trend should have no impact on the aggregate figures.

Unemployment Insurance

One common explanation for unemployment is that improved unemployment insurance benefits and coverage adversely affect workers' behaviour. By reducing the costs associated with unemployment, unemployment insurance benefits lengthen the duration of joblessness, reduce labour mobility, discourage the active search for work and increase job turnover. In a nutshell, unemployment insurance is said to increase voluntary unemployment.

Empirical studies have shown that the 1971 Unemployment Insurance Act revisions, which increased benefits relative to the average wage, were responsible for one to two percentage points increase in the unemployment rate.[23] The tightening of unemployment insurance regulations in 1979 had the opposite effect.

Yet some economists dispute the idea that social programs such as unemployment insurance increase structural or frictional unemployment. They argue that empirical studies measuring the impact of changes in the Unemployment Insurance Act ignore the aggregate demand effect of such changes, and hence the positive impact they must have on employment. The net effect of these changes may well be a reduction in unemployment. Moreover, they question how the unemployed could choose to remain unemployed, when it is obvious that there are not sufficient jobs available.

In any case, there have been no major changes in the Unemployment Insurance Act since 1979, so any subsequent rise in the unemployment rate cannot be attributed to this factor.

Excessive Real Wages (Classical Unemployment)

It has been argued that excessive real wages are the major cause of high unemployment today. This view, which has been quite popular in Europe, states that the real wage has tended to grow faster than labour productivity, leading to a rise in the labour share and a corresponding decline in the profit share of the national income. The main limit to the recovery in the past few years would be low business profitability, due to the excessive growth of real wages during the 1970s. Since the shift from profit to wages has damaged investment, a reduction in real wages would increase profits, raise investment and reduce unemployment.

The "real wage gap" is a statistical index of real wage changes minus labour productivity changes, which shows movements in the distribution of income between wages and profits compared to a base period. A positive real wage gap would reflect a rising share of national income going to labour and a

smaller share going to profits; a negative real wage gap would show the opposite.

Estimates of the real wage gap for Canada indicate that real wages have frequently fallen short of trends in labour productivity over the past ten years, and particularly in recent years.[24] These results may appear dubious, given that Canada's productivity performance has been very weak by historical standards. But the trend in real wages has been just as weak, or weaker. From 1978 to 1984, real wages in Canada declined in five years out of seven. Real wages, as measured by real labour income per paid employee, are now about five per cent below the peak established in 1977.

Some economists have argued that further real wage cuts are necessary.[25] They suggest a trade-off between real interest rates and real wage rates, and see high real interest rates as the main impediment to business profitability and investment growth. For various reasons, it is argued that nothing can be done in the short term to reduce real interest rates. Therefore, employment will only grow if business profitability is re-established through further cuts in real wages.

This argument assumes that investment decisions are determined by current levels of profitability. However, in making an investment appraisal, the firm will calculate its expected rate of profit. A key determinant of this rate is the expected future demand for the goods and services produced by the machine, plant or factory in which the firm plans to invest. If future demand is expected to remain depressed, and governments show little inclination to reverse this situation, the investment will not take place.

Furthermore, future demand is very strongly determined by income levels. Real wages are a key element in incomes, so if they are cut there will be less market for increased production and firms will not invest. As we have noted, Canada has experienced drops in real wages since 1978 which have not been accompanied by strong investment performance. Weak business investment in plant and equipment was a major drag on the recovery in Canada through 1983 and 1984.

Unions

During the recession, there was a great deal of publicity surrounding rollback agreements between unions and management in the United States, which are alleged to have restored the financial viability of certain companies and allowed them to maintain employment. Canadian unions have been criticized for not adopting a similar conciliatory attitude. It is often argued that unions should agree to lower nominal wages to reduce firms' costs, thereby allowing them to reduce prices, increase output, and create employment.

First, it must be pointed out that concessions in wages and benefits have been as important in Canada as in the U.S., but took place at a later date. In

1983, over 40 per cent of all workers signing contracts were affected by wage and/or benefit concessions. This proportion increased to 51 per cent in the first half of 1984.[26]

Second, the extent to which pay cuts result in lower prices, increased output, and new employment depends partly upon the market in which a firm sells its products. If demand is not very responsive to price, the firm will use wage cuts to increase profits rather than reducing prices or increasing employment.

Finally, as Keynes has shown, cutting wages is a self-defeating approach to new employment generation. Even if all workers were willing and able to work for a lower wage, employers would be unable to increase their volume in the absence of increased demand for their products. A general reduction in the money wage rate would reduce workers' disposable income, so that any additional goods and services that enterprises might produce could not be sold.

Minimum Wage Laws

Some economists and business representatives have maintained that increases in minimum wage rates have led to increased unemployment in Canada and in some provinces. A reduction in minimum wages, or measures to prevent further increases, would be particularly useful as a cure for unemployment, especially for youth unemployment.

Most studies of minimum wage legislation and employment growth in Canada and the United States have found little if any impact. However, the Macdonald Commission stated that rapid increases in minimum wages relative to prevailing average wage levels in the early 1970s had led to higher unemployment.

What might have been true for that period is certainly not true anymore. In 1974, the average provincial minimum wage was roughly half the average hourly wage rate for manufacturing in Canada. Since then, the average minimum wage has been eroded to 32 per cent of the hourly manufacturing wage. An immediate hourly increase of $2.07 would be required just to restore the average minimum wage to its former 50 per cent level. Any increase in unemployment that may have been due to minimum wages in the early 1970s has certainly been more than offset by these recent trends.

Other Labour Market Rigidities

It is often suggested that labour market rigidities are the major obstacle to any improvement in Canada's overall economic performance. The removal of such rigidities would be the first step in allowing the private sector to realize its full potential as a job generator. In addition to minimum wage laws, unemployment insurance benefits and unions, such factors as labour standards, government regulation, and payroll taxes are blamed for the sluggish

growth of employment and the limited decrease in unemployment rates since the depths of the 1981-1982 recession. This argument has relied heavily upon comparisons with the performance of the U.S. economy, where strong employment growth after the recesssion has been attributed to the greater "flexibility" of the American labour market.

Recent studies have found that changes in labour market rigidities do not explain the differences in labour market performance in the two countries.[27] Much lower aggregate demand in Canada has been identified as the major cause of labour market performance. Indeed, it is hard to detect any drastic change since the recession in the various factors that have been proposed as impediments to the labour market adjustment process. If there was no change, these factors can hardly be associated with increased unemployment.

From the foregoing it appears that, while a case can be made on economic grounds that insufficient aggregate demand is a fundamental cause of unemployment, it is much more difficult to substantiate the various non-cyclical explanations that have been advanced by various observers.

Conclusion

In this paper we have sought to present unemployment in all its major dimensions. It should be clear that the debate over policies to deal with unemployment is much wider than our discussion of the nature, costs, and causes of unemployment. Ultimately, the unemployment debate should deal with the quality of work and the problem of underemployment, as well as the more quantifiable features of job creation and job losses.

Perhaps the most significant question of all has to do with the meaning of unemployment in a democracy. In its broadest sense, democracy requires that public opinion be well informed. For democracy to flourish, it is not enough that there be a consensus among experts about the best technical approach to a social question like unemployment; there must also be a broad understanding within society at large about what is at stake in the debate over unemployment. When experts cannot even agree on the fundamental causes of unemployment, does this then mean that the public has no basis for deciding the issue, and that public debate is fruitless without an expert consensus?

For organizations like the Social Planning Councils of Canada, there can be no *expert* debate without public participation in the discussion. The meaning of the unemployment situation cannot be decided until public opinion has been expressed. This requires that public policy analysis not take place in a rarified atmosphere, where only expert opinion is admitted. It requires that the views of the public be sought and heeded. It entails a process in which the agenda for decision-making is as democratic as possible.

From this perspective, one way of interpreting unemployment in Canada is to say that the current situation is a matter of choice — that Canadians,

through their leaders and political parties, have allowed an unprecedented post-war level of unemployment to develop, largely because public opinion has not condemned the existing state of affairs. In other words, unemployment is a political problem, not a technical one.

We have attempted to show, on economic grounds, that high levels of unemployment are likely to persist unless significant changes are introduced by governments at all levels. Moreover, the problem is much wider and deeper than the frequently cited official unemployment rate would suggest. Hidden forms of unemployment, and the incidence and duration of unemployment, reveal the true scope of the problem we are facing.

The costs of unemployment are much greater than is generally understood. Considering only the relatively narrow economic costs inherent in persistent unemployment, it is no exaggeration to classify any economic policy that does not directly reduce unemployment as a second-best strategy. When the social and individual costs are considered as well, and we argue that they must be considered seriously, the argument for acting against unemployment takes on a real urgency.

In our view, the debate on unemployment must become a job creation debate. The question of whether to stimulate job creation has already been answered by public opinion. In a democracy of the calibre to which Canada aspires, citizens have a responsibility to share their views and knowledge. Those who oppose unemployment have a responsibility to make society aware of full employment alternatives.

NOTES

1. For a survey of international trends in unemployment see J. Moy, "Recent Trends in Unemployment and the Labour Force, 10 countries," *Monthly Labor Review*, August, 1985 and OECD *Economic Outlook*, December 1986.
2. An additional form of underemployment is over-qualification of workers for jobs.
3. For a detailed analysis of the measurement of hidden unemployment, as well as other labour market issues, see A. Hasan and P. de Broucker, *Unemployment, Employment, and Non-Participation in Canadian Labour Markets* (Ottawa: Economic Council of Canada, 1985).
4. For a detailed analysis of youth employment see David Ross, *Youth Economic Activity*, (Ottawa: Department of the Secretary of State of Canada, December, 1984).
5. P. Shaw, "The Burden of Unemployment in Canada", *Canadian Public Policy*, June, 1985.

6. Cat. 71-001, March 1986, Statistics Canada.

7. Shaw, "The Burden of Unemployment", op. cit..

8. See A. Okun, ed., *The Battle Against Unemployment*, (New York: W. W. Norton, 1972).

9. For a discussion of this concept see ch. 3, D. Bellemare and L. Poulin Simon, *Le plein emploi: Pourquoi?* (Quebec: Presses de l'Université du Québec, 1983). The Okun coefficient is based on three phenomena: (1) when unemployment falls, employment increases more than proportionally due to higher participation rates; (2) when unemployment decreases, average weekly hours increase due to overtime and replacement of part-time workers by full-time workers; and (3) when unemployment decreases, productivity increases.

10. See for example M. Jahoda, *Employment and Unemployment: A Socio-Psychological Analysis* (London: Cambridge University Press, 1982); Canadian Mental Health Association, *Work and Well-Being -- The Changing Realities of Employment* (Ottawa: 1984); and D. Bellemare and L. Poulin Simon, *Le plein emploi: Pourquoi?* (Quebec: Presses de l"Université du Québec, 1983).

11. See Paul Phillips, *Unemployment Insurance and Jobs: A Review of the Issues*, paper prepared for the National Economic Conference, March, 1985.

12. *Royal Commission on the Economic Union and Development Prospects for Canada, Volume Two* (Ottawa: 1985), p. 10.

13. A. Hasan and P. de Broucker, *Unemployment, Employment and Non-Participation in Canadian Labour Markets* (Ottawa: Economic Council of Canada, 1985), p. 90.

14. See D. Bellemare and L. Poulin Simon, *Le plein emploi: Pourquoi?* (Quebec: Presses de l'Universtié du Québec, 1983), for a good example of this view.

15. See A. Raynauld, "La politique fiscale et le chômage", *L'Actualité Economique*, December 1984, and R. Tremblay, "Les causes structurelles du chômage actuel", *L'Actualité Economique*, December 1984. Tremblay estimates that the non-cyclical rate of unemployment is currently around nine per cent.

16. Royal Commission on the Economic Union, *Vol. 2*, p. 315.

17. See Hasan and de Broucker, op. cit..

18. The term 'structural unemployment' is often used in the economic literature to designate all types of unemployment that are neither cyclical nor frictional. Here, the term is used in a narrower sense.

19. Royal Commission on the Economic Union, *Vol.* 2, pp. 76-77.
20. For an overview of this question see S.F. Kaliski, "Why Must Unemployment Remain So High?", *Canadian Public Policy*, June 1984.
21. F. Reid and D. A. Smith, "The Impact of Demographic Changes on Unemployment", *Canadian Public Policy*, 1981, Vol. II, pp. 348-351.
22. F. Reid and D. A. Smith, op. cit..
23. See Kaliski, "Why Must Unemployment Remain So High?"
24. See for example Jacques R. Artus, "An Empirical Evaluation of the Disequilibrium Real Wage Hypothesis", *National Bureau of Economic Research*, Working Paper No. 1404, July 1984.
25. Rodrigue Tremblay, "Les causes structurelles du chômage actuel".
26. See J.-P. Voyer, *Recent Trends in Wages: Is the Slowdown Purely Cyclical?*, NUPGE Research Report No. 4, June 1985.
27. M. Gunderson and N.M. Meltz, *Labour Market Rigidities and Unemployment in Canada*, paper presented at the conference, Unemployment: Can It Be Reduced? An International Perspective, University of Toronto, November 28-30, 1984.

II

*THE STATE AND LABOUR MARKETS: TOWARDS A COMPARATIVE POLITICAL ECONOMY OF UNEMPLOYMENT**

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In the western capitalist world, one of the prevailing images of post-war politics has been that of the rise and decline of a Keynesian consensus. With the decline in this consensus, based in part on the objective of full employment, the spectre of mass unemployment has returned.

These events have posed a variety of theoretical and practical questions both for those involved in the political process and for social scientists. These include understanding the causes and consequences of the unemployment crisis, anticipating the likely future course of events, and devising appropriate programmes. This article surveys two bodies of literature which have addressed these questions, and which highlight the range of responses occasioned by the return of mass unemployment.

The first, which can be characterized as the "Post-Employment Society" school, is exemplified by the recent works of Gorz, Keane and Owens, and Offe.[1] To state this school's argument at its maximum, a return to full employment is considered to be neither feasible or desirable. Instead this school draws its inspiration from utopian socialist writers, whose solution to unemployment was to reduce or abolish society's "fetishism of paid labour".[2] To

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confront the phenomenon of mass unemployment, socialists are called upon to invent "viable strategies for ending the tyranny of paid work, thereby making possible a post-employment society which maximizes individuals' choice of whether, or how much, they work for pay".[3]

The second approach, which I characterize as the "Full Employment Society" school, is represented in a recent book by Therborn.[4] Adopting an approach that is historical, materialist and comparative, this school takes as its starting point the observation that the impact of unemployment has, in fact, been quite diverse. Some countries have maintained full employment rather well, while others have slumped into mass unemployment situations. The obvious question is "why?" Therborn's precise answer to this question will be dealt with at greater length below. But it can be noted that his principal finding is that politics and policies are important for an explanation of variations in levels of unemployment, politics and policies. Unemployment levels to a considerable extent are determined by political choices, past and present. This leads Therborn to a discussion of two alternative future scenarios. In one, termed 'Brazilianization', mass unemployment and increasing marginalization will be the lot of large numbers of the population. The other, 'the labour comeback scenario', envisages policies designed to bring about a return to full employment while satisfactorily addressing issues such as women's participation in the labour force and the need to reduce environmental pollution.

Provided these conditions are met, Therborn considers that "all ideologies which attack the goal of full employment should be relegated to where they belong — explicitly or by implication — in the arsenal of the Brazilian ruling class".[5] Writing as a socialist as well as a political scientist, Therborn is at some pains to emphasize that the labour comeback scenario is not a socialist one, though it might establish conditions which would make advances toward socialism possible — a result which will not be achieved by "people on the dole."

Given this basic dichotomy between the two schools of thought, a further elaboration of each is justified. These ideas have considerable Canadian relevance, given the 'conventional wisdom' that the route to economic health (including, at least at the level of rhetoric, more jobs) lies in less government, deficit reduction, and so on. Therborn's comparative study indicates that appropriate government policies *can* lead to full employment. It also indicates that the policies currently being pursued in Canada lead in the opposite direction. In this sense, Michael Wilson, together with his colleagues and predecessors, can be regarded as practitioners of a right-wing version of the post-employment society scenario.

Towards a Post-Employment Society?

Of the three examples of this perspective discussed here, Claus Offe is by far the most sophisticated. His analysis is grounded in the argument that work,

labour and class are no longer the central facts of life in capitalist society.[6] The increased structural differentiation and dualism of labour markets provide Offe with illustrative material for this thesis.[7] He notes that no more than half the population normally participates in labour markets, and argues that a tendency to exclude increasing numbers of people is part of both state and trade union strategy. Even for those within the labour market, work itself has become so differentiated that those composing the category 'employee' in fact have little in common. The result of these trends, both for those in and those outside the labour market, is that work is "forfeiting its subjective role as the central motivating force in the activity of workers".[8] Even in the absence of these value changes, however, Offe depicts labour markets as absorbing a smaller and smaller proportion of the population for the foreseeable future. A variety of economic, demographic, political and ecological factors mean that the 'years of plenty' are over, and the value changes referred to either reflect or reinforce this situation.[9] Even if investment and growth were to revive somewhat, Offe sees little or no impact on the provision of job opportunities.

The consequence of this analysis is the prediction that "a growing proportion of the population in age groups capable of productive work will have to be provided with an income by means of something other than the 'sale' of their labour power".[10] Offe recognizes that such minimum income or guaranteed annual income provisions might be insufficient to lead to satisfactory lives for those receiving them, and that however generous, such schemes deny the need for creative human activity.[11] The solution, he argues, lies in the political encouragement and provision of conditions in which "people can supply themselves with goods and services without having to purchase them...This type of informal or 'decommodified' provision of benefits consists of use-values which can substantially supplement and improve the level of material well-being that individuals and households attain through monetary income. The informal provision of goods and services has the additional advantage of ensuring that those parts of the labour potential which cannot be accommodated in the labour market are utilized in a self-determined way, and are not condemned simply to passivity".[12] For Offe, given that learning to cope with increasing mass unemployment will be a long-term phenomenon, the only choice about the post-employment society is whether it will be the bleak wasteland likely to result from laissez-faire processes, or a more benign and politically structured experience.[13]

Essentially the same conclusion is reached by the other authors under discussion. Keane and Owens argue that employment societies, "in which most people, for at least some of their lives, work for a wage or salary within a labour market", are historical aberrations.[14] Be this as it may, they consider that the post-war full employment experience "is not repeatable"[15] and that the unemployment crisis provides socialists with "a once-in-a-lifetime opportunity"[16] to create a post-employment society along the more benign lines identified by Offe. Similarly, Gorz finds that the process of abolishing work

(i.e., paid work) is already occurring and is likely to accelerate,[17] that Keynes is dead,[18] and that the only choice is "*either* a socially controlled, emancipatory abolition of work *or* its oppressive, anti-social abolition".[19] For these writers, as for Offe, an essential ingredient in the construction of the post-employment society is some form of guaranteed income or social wage.[20]

The vision of the future advanced by these writers can be criticized on a number of grounds. First, their failure to specify the transformation process to a benign post-employment society is rather serious. Unless one is convincingly told *who* will ensure that guaranteed standards of life in a post-employment society will be adequate, and *how* this will be achieved, there is no reason to suppose that such a society would resemble anything other than the universalization of Liverpool's experience. Gorz's assertion that such a society will be introduced with the support, though not the active agency, of a "non-class of non-workers" is simply ludicrous and quite literally beyond belief.[21] The silence of the other authors on this issue is scarcely more impressive. Second, their interpretation of empirical trends within contemporary capitalism, and their repudiation of the centrality of work, labour and class are open to serious objections at both empirical and theoretical levels.

Neither of these critiques, however, provide the focus of this article, which concentrates on the alleged *consequences* of the developments described by the post employment theorists. A central feature of their argument is that a return to full employment capitalism, whether one regards that as desirable or not, is impossible. In contrast to that argument, this article explores the notion that full employment capitalism remains a possibility. The empirical observation that something like it continues to exist in certain countries tends to support this perspective. Notwithstanding the pressures on full employment emanating from the imperatives of capital accumulation, it remains both feasible and desirable. In this context, Therborn's book — rigorously grounded in historical and contemporary empirical analysis, and eschewing false optimism about labour market possibilities — provides a realistic and challenging antidote to the dismal prognoses outlined above.

The Necessary Conditions of Full Employment Society

Therborn's starting point is the observation that some countries have a higher rate of unemployment than others. In fact, some countries manage to combine low unemployment, high rates of growth in employment, and high levels of labour force participation, while other countries experience the opposite. To be more systematic about this, Therborn uses these three indicators to rank 16 OECD countries in terms of their success from a labour point of view.[22] Unlike the writers previously discussed, Therborn, writing from a class analysis perspective, has no problem in unambiguously identifying full employment with the interests of the working class. Three broad categories of national experiences are identified: successes — Norway, Sweden, Japan, Austria and Switzerland; failures — Denmark, Canada, Italy, Britain, the

Netherlands and Belgium; and an intermediate group consisting of Finland, the U.S., Australia, France and West Germany.

The study examines[23] the extent to which these differences in performance can be explained in terms of general economic or universal market factors.[24] The analysis reveals only small or, in some cases, non-existent relationships between poor performance in the employment area, and a host of other factors whose potential significance is derived from conventional economic theory. These include: economic growth; labour force growth; labour-saving investments and technological change patterns; inflation; export performance; size of the service sector; profits; labour costs; levels of social expenditure; and, levels of unemployment compensation. Rejecting conventional economic explanations of variations in unemployment levels, Therborn then turns to nationally specific factors and, in particular, to what he terms the "national politics of economics".[25]

In seeking explanations in the political and institutional realm, Therborn is, of course, in the company of a number of other writers.[26] Generally this type of explanation has focussed either on social democratic predominance in government,[27] or on the existence of corporatist institutions.[28] Therborn is somewhat critical of both explanations[29] and offers as an alternative, "the existence or non-existence of an institutionalized commitment to full employment". By this he means: (a) an explicit commitment to maintaining/achieving full employment; (b) the existence and use of countercyclical mechanisms and policies; (c) the existence and use of specific mechanisms to adjust supply and demand in the labour market to the goal of full employment; (d) a conscious decision not to use high unemployment as a means to secure other policy objectives.[30]

He detects two major and quite different routes by which the full employment commitment became institutionalized in various countries. In some, it resulted from the assertion of working class interests by strong labour movements. In others, the origins lie in the bourgeoisie's conservative concern for order and stability.[31] Whatever its origins, however, the institutionalization of the full employment commitment implies that politics and, above all, *policies* matter.[32] Constraints and pressures upon policy makers are not ignored but the point is made that "policy constraints are not simply given. They are to a great extent politically and ideologically defined by the power relationships which determine policy priorities and which have been left as a legacy from the past".[33]

Therborn's concept of an institutionalized commitment to full employment thus incorporates ideological and policy choices, as well as the power relationships which lie behind them, and which are, in a sense, embodied in them.

Three types of policy — and the direction these policies might take — are selected for comparison in the sixteen countries which comprise Therborn's sample. These are: (1) fiscal policy, which may be expansionary or

restrictive; (2) monetary policy, which can be loose or tight; and, (3) labour market policies, which can be classified as preventive, restrictive or compensatory. The policy profiles of the sixteen countries are then presented. The conclusions, as far as the five successful countries — those which have maintained full employment — are as follows[34]: (1) All the successful countries pursued expansionary Keynesian policies in the depth of the post-1973 crisis, and on some occasions since then; (2) None of these countries relied exclusively on such measures. Complementary monetary policies, in particular low real interest rates, and direct interventions into the market economy were also followed; and, (3) There was, however, considerable variety in the type of direct intervention utilized. In Sweden, it took the form of active labour market policies such as public works and job training. At their peak, these measures reduced the Swedish unemployment rate by about four percentage points. Norway emphasized public subsidization of private sector employment. In Switzerland, the key instrument was immigration control, which essentially consisted of the expulsion of foreign workers. Austria relied on maintaining public investment, restricting immigration, and a tight incomes policy. In Japan, import restrictions and direction of credit were most significant. Obviously not all of these policy instruments are equally desirable from a labour perspective. The particular choice of measures no doubt reflects the class origins of the full employment commitment. But the more general point is that in addition to endorsing Keynesian demand management, and in some cases ensuring a compatible monetary policy, the state in the full employment countries "has significant control of one or more strategic economic variables on the market itself, a control which has been amply used to ensure full employment. This has meant control of labour supply in Switzerland and Austria; of labour demand and of qualitative labour supply in Sweden; investment in Japan, Austria and Norway; and price and cost structures in Norway and Austria".[35]

In those countries where full-employment has lapsed, a number of common themes stand out amidst considerable policy variety.[36] First, contradictory policies which tended to cancel each other out were followed (e.g., Denmark, France, West Germany). Second, labour market policies tended to emphasize compensation for unemployment, rather than its prevention (e.g., Denmark, West Germany, Netherlands). Third, in some cases (e.g., Britain, Belgium) maintaining full employment does not seem to have been an objective. In all cases, these policy choices are traced to the absence or weakness of an institutionalized full employment commitment.

Not all of Therborn's conclusions are uncontroversial.[37] Nevertheless the pattern emerging from his study does lend credibility to the argument that the policies pursued in various countries are strongly connected to the levels of unemployment they experience. In this sense, unemployment, or its absence, is to a considerable extent a matter of political choice. The main qualification to this is that the choices made should be understood as being rooted in historically institutionalized power relationships.

Therborn does not devote a great deal of attention to Canada specifically. There is, however, sufficient evidence available to suggest that his general approach to the reasons for unemployment holds true in this country. As in many other western countries, the Canadian state in the post-war period proclaimed its commitment to the use of macroeconomic policy for maintaining "high and stable levels of employment".[38] If this was generally interpreted as meaning full employment, there have been grounds for disappointment. In comparison with most other advanced capitalist countries, Canada's unemployment rate remained stubbornly high throughout the long post-war boom.[39] Nevertheless, until the mid-1970s, the federal government's macroeconomic policy either produced or at least was consistent with unemployment levels that were low by Canadian standards.

From 1975, the goals and means of macroeconomic policy in Canada changed. The Bank of Canada announced a policy of decreasing the rate of growth in the money supply, and as part of its Anti-Inflation Programme, the federal government became committed to fiscal and monetary policy in the fight against inflation. A key element in this strategy was a restriction on the growth of government expenditures to a rate less than the growth rate of the GNP.[40] The progressive tightening of money supply targets, combined with other measures, contributed to economic depression and rising unemployment in the late 1970s.[41] Similarly, the anticipated persistence of high unemployment has been attributed not only to the depth of the recession, but also to the deliberately slow speed of economic recovery, which was planned with control of inflation in mind.[42]

In the more specific areas of labour market and job creation policy, the pattern is the same. Notwithstanding considerable rhetoric about job creation and a plethora of actual programmes, the real priority accorded this policy area seems to have declined since the onset of economic crisis in the mid-1970s.[43] Although there were some fluctuations in individual years, *real* expenditures on job creation declined over the decade 1972-82, and fewer jobs were created — both in absolute terms, and as a percentage of the labour force. The Canadian state, therefore, responded to economic crisis with a restrictive macroeconomic policy, and without any expansion of compensatory measures in specific policy areas such as job creation. This policy response constitutes Canada's route to high unemployment, and it is consistent with the policies adopted in the other high unemployment countries which Therborn analyzes in more detail.

One major effect of Therborn's work is to modify the image of post-war western politics as the rise and fall of a Keynesian consensus, and, as its concomitant, the rise and fall of full employment capitalism. Therborn is, of course, not the first social scientist to draw attention to this. Nixon Apple, for example, has argued that much of the post-war commitment to full employment, which derived from Keynesianism, was more apparent than real.[44] Obviously the image itself remains a useful one in that it identifies the trend of events in most capitalist countries as well as the tendencies and pressures

experienced in all of them. But, like any generalization, it masks very real variations in national experiences.

The continued existence of considerable pockets of full employment suggests that the image is somewhat overdrawn, and in any case that apocalyptic visions of the end of 'employment society' are vastly exaggerated. In my opinion, the superiority of Therborn's approach derives, empirically and theoretically, from the comparative nature of his investigation, and from the fact that it is rooted in a class analysis perspective. Had the post-employment society theorists conducted systematic comparative research, their certainty about the universality of the empirical trends they identify must have been considerably reduced. It is surely not fanciful to suggest that their failure to conduct an adequate comparative investigation is related to their retreat from class analysis. This is perhaps most obvious in the case of Gorz, who regards the employment society and its associated class structure with such distaste, and is in such haste to bid the working class farewell, that inconvenient facts tend to be ignored.[45]

Therborn, operating from a working class or labour perspective, regards the desirability of full employment as obvious.[46] Far from leading to self-indulgent wishful thinking however, this evaluation leads to a rigorous search for an understanding of those conditions which sustain full employment, and, on the other hand, for those conditions which tend to undermine it. The resulting comparative analysis makes a major contribution to our understanding of the linkage between the balance of political forces within countries, ideas and state policies, and the performance of national economies.

In any event, to have demonstrated that full employment continues to be a *possibility*, and *how* that possibility might be realized, puts the case for a post-employment society on a different footing. Rather than relying on the argument that this is an inevitable development — "there is no alternative" — it becomes incumbent on its advocates to argue for its *desirability* in a world where other options are available. An integral part of such an argument would be a demonstration of the process by which a transition to a benign post-employment society might occur. The failure to provide this is a major theoretical flaw. In the absence of a convincing theoretical resolution of such problems, the practical achievements of the post-employment theorists are likely to be about as great as those of their utopian socialist antecedents.

If the decline of full employment has been less universal than the prevailing image suggests, the same can be said about the relevance of Keynesian ideas. While Therborn concedes that the 1970s "shattered the complacency of simple-minded Keynesianism",[47] it remains true that in all cases where full employment was sustained, expansionary Keynesian fiscal policies did play some role. It is in fact fairly clear that the Keynesian consensus was itself nationally variegated, and that the more successful versions seem to have paid attention to the stimulation of investment as well as consumer demand, and to synchronizing fiscal expansion with monetary and exchange rate

policy. Whether such policies will ultimately prove successful in sustaining full employment remains to be seen. Though Therborn emphasizes the role of politics and policy, he stops well short of suggesting that these factors enjoy an absolute autonomy from structural influences. But what is absolutely clear is that the power of resistance of such policies, where an institutionalized commitment to full employment existed, was far greater than the experience of "simple-minded Keynesianism" — so readily abandoned in some countries — would suggest. From this we might infer that the state's autonomy from structural constraints is sufficiently significant as to render the 'post-employment society' school's surrender to market forces premature, if not unnecessary.

Another noteworthy point emerging from Therborn's discussion is that despite the nationally specific features of full employment strategies, all seem to rely on strong, national-level, state intervention — a fact that gives one pause for thought, given the current fashionability on the political left of calls for decentralization and reductions in the role of the central state.

Finally, having outlined two scenarios — 'Brazilianization' and 'labour comeback' — Therborn is content to concede that both are possible for the countries under discussion. His book is an exploration of possibilities. As such it provides a refreshing contrast to the determinism of the post-employment society theorists. And through its emphasis on policy and the politics of unemployment, it provides an essential ingredient to the political economy of the subject, which can offer some guidance to those committed to reversing the trends towards mass unemployment so apparent in many capitalist countries.

NOTES

1. Andre Gorz, *Farewell to the Working Class* (London, 1982); John Keane and John Owens, *After Full Employment* (London, 1986); and, Claus Offe, *Disorganized Capitalism*, ed. John Keane (Cambridge, Mass., 1985).
2. Keane and Owens, *After Full Employment*, p. 161. (See n. 1, above.)
3. Ibid., p. 178.
4. Goran Therborn, *Why Some Peoples Are More Unemployed Than Others: The Strange Paradox of Growth and Unemployment* (London, 1986).
5. Ibid., p. 36.
6. Offe, *Disorganized Capitalism*, Chapter 5. (See n. 1, above.) A detailed consideration of the 'beyond class' thesis is beyond the scope of this article. For an excellent critique of leftist attempts to de-class Marxist analysis, see Ellen Meiksins Wood, *The Retreat from Class: A New 'True' Socialism* (London, 1986).

7. Offe, *Disorganized Capitalism*, pp. 33-35, 47.
8. Ibid., p. 148.
9. Ibid., pp. 60-63.
10. Ibid., p. 65.
11. Ibid., p. 99.
12. Ibid., p. 100.
13. Ibid., p. 80.
14. Keane and Owens, *After Full Employment*, pp. 11-15.
15. Ibid., pp. 7-8.
16. Ibid., p. 178.
17. Gorz, *Farewell to the Working Class*, p. 3. (See n. 1, above.)
18. The result of a self-fulfilling prophecy?
19. Gorz, *Farewell to the Working Class*, p. 8.
20. Keane and Owens, *After Full Employment*, pp. 176-177.
21. See Wood's discussion of Gorz in *The Retreat from Class*, pp. 15-18. (See n. 6, above.) The failure to specify such a transforming process, Woods aptly comments, means that Gorz's work is both "utopian vision and counsel of despair".
22. Therborn, *Why Some Peoples Are More Unemployed*, Chapter 11. (See n. 4, above.)
23. Ibid., Chapter 1.
24. A number of these factors, such as technological change and demographic pressures, are used by the post-employment society theorists to justify their claim that no return to full employment is possible.
25. Therborn, *Why Some Peoples Are More Unemployed*, p. 41. Obviously the rejection of conventional economic explanations will be controversial in some quarters.
26. Notable among them are: Nixon Apple, "The Rise and Fall of Full Employment Capitalism," *Studies in Political Economy* 4 (Autumn, 1980), pp. 5-39; David R. Cameron, "Social Democracy, Corporatism, Labour Quiescence and the Representation of Economic Interest in Advanced Capitalist Society," in *Order and Conflict in Contemporary Capitalism*, ed. John H. Goldthorpe (Oxford, 1984), pp. 143-178; Douglas Hibbs, "Political Parties and Macroeconomic Policy," *American Political Science Review* 71 (1977), pp. 1467-1487; Fritz W. Scharpf, "Strategy Choice, Economic Feasibility and Institutional Constraints as Determinants of Full

Employment Policy During the Recession," *Public Policies to Combat Unemployment in a Period of Economic Stagnation: An International Comparison*, eds. K. Gerlach, W. Peters and W. Sengenberger (Frankfurt, 1984), pp. 67-114; and Manfred G. Schmidt, "Does Corporatism Matter? Economic Crisis, Politics and Rates of Unemployment in Capitalist Democracies in the 1970s," in *Patterns of Corporatist Policy Making*, eds. Gerhard Lehmbruch and Phillipe C. Schmitter (London, 1982), pp. 237-258.

27. For example, Hibbs, "Political Parties and Macroeconomic Policy". (See n. 26, above.)

28. For example, Schmidt, "Does Corporatism Matter?" (See n. 26, above.)

29. Therborn, *Why Some Peoples Are More Unemployed*, pp. 96-101.

30. Ibid., p. 23.

31. Ibid., pp. 23-25.

32. A point also made by Scharpf.

33. Therborn, *Why Some Peoples Are More Unemployed*, p. 94.

34. Ibid., pp. 101-111, and 23-30.

35. Ibid., p. 28.

36. Ibid., pp. 132-162.

37. For example, his assessment of French policy: "The Mitterand government has failed to keep unemployment down, mainly because of its own contradictory policies...The main reason for the miserable French employment record from 1981 to 1984 is to be sought in historically institutionalized patterns of politics, not in economic theory or international dependence". Ibid., p. 143.

38. Department of Reconstruction, *White Paper on Employment and Income* (Ottawa, 1945).

39. Arnold J. Heidenheimer, Hugh Heclo and Carolyn Teich Adams, *Comparative Public Policy: The Politics of Social Choice in Europe and America*, 2nd edition (New York, 1983), p. 123.

40. On this change of strategy see two works by David Wolfe: "The Rise and Demise of the Keynesian Era in Canada: Economic Policy, 1930-1982," in *Modern Canada 1930-1980s*, eds. Michael S. Cross and Gregory S. Kealey (Toronto, 1984), pp. 46-78; and "The Politics of the Deficit," in *The Politics of Economic Policy*, Research Coordinator, G. Bruce Doern (Toronto, 1985), pp. 111-162.

41. Arthur W. Donner and Douglas Peters, *The Monetarist Counter-Revolution: A Critique of Canadian Monetary Policy, 1975-79* (Toronto, 1979);

John McCallum, "Monetarism in Three Countries: Canada," in *Beyond the Monetarists*, ed. David Crane (Toronto, 1981), pp. 48-62.

42. S.F. Kaliski, "Why Must Unemployment Remain So High?", *Canadian Public Policy* 10 (1984), pp. 127-141.

43. For a substantiation of this point, see Stephen McBride, "Trends and Priorities in Job Creation Programmes: A Comparative Study of Federal and Selected Provincial Policies," in *The Canadian Welfare State: Evolution and Transition*, ed. Jacqueline S. Ismael (Edmonton, forthcoming 1987); Leon Muszynski, "The Politics of Labour Market Policy," in *The Politics of Economic Policy*, pp. 251-305 (see n. 40, above); and Douglas A. Smith, "The Development of Employment and Training Programmes," in *How Ottawa Spends 1984*, ed. Allan M. Maslove (Toronto, 1984).

44. Nixon Apple, "The Rise and Fall of Full Employment Capitalism". In Britain, an extensive debate has occurred over whether there ever existed a thorough-going Keynesian revolution in policy which could decline and come to an end. Much of this debate can be traced in *Economy and Society* from 1981 onwards.

45. The tide of Gorz's subsequent work, *Paths to Paradise* (London, 1984), perhaps is indicative of a decreasing concern on his part with the realities of social existence.

46. As he points out, full employment also seems a desirable goal from at least some bourgeois perspectives.

47. Therborn, *Why Some Peoples Are More Unemployed*, p. 40.

Industrial and Employment Policy:
What are the Options?

In recent years, Diane Bellemare and Lise Poulin Simon have been engaged in one of the most important research programs undertaken by Canadian economists. In two major books, *Le plein emploi: Pourquoi?* and *Le défi du plein emploi*, they have drawn the parameters of full employment strategy in a world economy troubled by a major shift in the international division of labour, a crippling inflation crisis, and a loss of confidence in government's capacity to act in the public good. Their research is based on comparative analysis of European and Canadian circumstances. We are pleased to be able to present this article, drawn from their second book, which is one of the first English translations of their work.

While noting the importance of what Bellemare and Poulin Simon have to say, David Wolfe and Gilles Paquet both make significant comments of their own. In discussing the article, Wolfe points out that political circumstances in Canada diverge sharply from the European situation. He finds that the technical discussion engaged in by economists of the Macdonald Commission variety obscures the fact that employment policy is fundamentally a political matter. In his view, political mobilization is a prerequisite to full employment.

Paquet finds much to admire in the article. He points to the emphasis on flexible policy and comparative research as qualities worthy of emulation by others. But he is discouraged by the apparent importance of "security" for many Canadians. Given the nature of international markets, he believes that policy commitments which respond to this desire will leave Canada in an untenable position.

III

*FULL EMPLOYMENT: A STRATEGY AND AN OBJECTIVE FOR ECONOMIC POLICY**

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For more than 15 years, the unemployment rate in Canada and Quebec has been abnormally high. Moreover, the marked deterioration in employment opportunities since 1975 augurs poorly for any improvement in the immediate future. When federal and provincial governments have avoided policies likely to further increase unemployment rates, such as cuts in social expenditures, they have justified their inaction on the unemployment front by claiming that full employment is an impossible goal. It is in this context of job shortages that the Royal Commission on the Economic Union and Development Prospects for Canada was created on November 5, 1982, to study the political and economic options open to Canada. Its extensive report, presented to government on September 5, 1985, not only exhibited deep pessimism concerning full employment, but also signalled the abandonment of the pursuit of this objective.

Unable to anticipate automatic improvements in the employment situation over the next few years, the commissioners proposed that income growth,

* This article was first published in French in Économies et Sociétés, No.14, 1986.

rather than full employment, be adopted as the chief objective of Canadian economic strategy — even though employment was cited as the primary concern in most briefs to the commission.[1] The commission's recommended policy focus on market forces carries the strong risk of worsening the general employment situation, and doing so dramatically for groups such as youth and women, whose position in the labour market is already precarious.

As well, the commission called for significant changes to labour market institutions which, if implemented, will increase the segmentation of the labour market by identifying two categories of unemployed. The "not truly unemployed", who are deemed responsible for their economic condition by virtue of their own erratic behaviour in the job market, would exchange the right to unemployment insurance for a meagre guaranteed minimum income program which would inevitably perpetuate the shackles of poverty. The "truly unemployed", who have held stable jobs in the past, would retain sole right to unemployment insurance.

With this type of reasoning, there is a real danger that economic debate will focus narrowly on ways of transforming Canadian institutions to cope with high unemployment rates. With the philosophy of the Macdonald Commission driving Canadian policy, the abandonment of the objective of full employment that began in the 1960s will become complete. Yet full employment is not only an equitable objective, but can also form the basis of an economic development strategy. This, among other things, is what we set out to demonstrate in our book, *Le défi du plein emploi: un nouveau regard économique.*

Our work, summarized here, presents an alternative to the notion that free trade and heightened market competition will automatically bring about full employment. We begin with a historical analysis of the failure of Canadian economic policy since 1945 with regard to employment, and identify the reasons for this failure. Next, we compare the economic policies adopted since 1975 in Sweden, Norway, Austria and West Germany, to introduce four necessary conditions for a successful full employment strategy. Finally, we present a theoretical analysis that, by incorporating certain hypotheses in a basic Keynesian model, explains why these four conditions are essential. In the following pages, we draw together conclusions from the three types of analysis, more fully developed in our book.

LESSONS FROM THE CANADIAN EXPERIENCE

As in many other countries, the federal government promised Canadians after the Second World War that it would provide for a high level of national employment. It proposed to accomplish this through the appropriate management of the various components of aggregate demand,[2] based on the influence of Keynesian theory. But historical analysis shows that Canadian policy did not respect this commitment in practice.

With respect to employment, it is possible to identify three periods in the contemporary management of economic policy. The first period, from 1945 to 1956, was marked by Keynesian management of a macro-economic nature. The federal government exercised responsibility for general economic policy, utilizing four main instruments to maintain sufficient aggregate demand to generate a high employment rate.[3] First, income security programs were developed, including unemployment insurance (1940), family allowances (1944) and old age security (1951), to support and stimulate consumption. While the advent of the welfare state is often associated with Keynesian demand management policy, the economic logic underlying the rapid growth of the welfare state during this period extended beyond Keynesianism.[4]

A second instrument of macro-economic stimulation was a residential construction policy in which the federal government established subsidies and provided loans at rates below the prevailing level, with adjustments as circumstances required. Public investment constituted the third element of demand management. Finally, a general policy of low interest rates was one further instrument of macro-economic policy.[5]

Beginning in 1957, federal strategy underwent a number of changes which continued to guide policy until 1974. Economic policy, which until then had been almost exclusively macro-economic in character, was transformed into a combination of macro and micro-economic measures. Rather than managing demand through measures applicable to all economic sectors, the government adopted targets and designed specific policies to meet them.

During this period, two schools of thought were converging to justify the use of a more moderate macro-economic policy, in conjunction with micro-economic instruments to stimulate the economy. The structuralists attributed a large share of unemployment to inadequate adjustments between regional demand and opportunities for work, in both occupations and industries. According to this view, it was useless to attempt to rectify the problem of unemployment through expansionist macro-economic policies because of the inflationary pressures they might generate. Some Keynesians, meanwhile, stressed that inflation caused by macro-expansionary policies could gallop out of control. In Canada at this time, price increases, while moderate in today's context, still generated much worry that inflation not increase.

These two schools of thought presented the federal government with the justification to adopt a macro-economic policy which, from the perspective of the budgetary concept of full employment, could be qualified as neutral if not deflationary. In return, micro-economic measures and programs were developed to stabilize employment. Professional training, mobility, and temporary job creation programs were deemed more suitable than efforts to stimulate demand. Programs to develop regions with high unemployment rates were also put in place, although these were less important than labour market programs.

Since 1975, macro-economic policy has gradually become more restrictive. Canadian policy has focussed on micro-economic instruments, and the monetary theory of the Chicago school, to the extent that the Keynesian economists responsible for Canadian policy appear to have become monetarists and abandoned the objective of full employment. Many of these new monetarists believe that full employment is impossible to achieve in Canada. For them, as for the conservatives, inflation and the danger of inflation are the chief enemies to combat. In this light, it is hardly surprising that unemployment has climbed rather drastically in Canada. Despite the evident importance of the international crisis, domestic policy decisions have played a role as well.

It is important to consider why Canadian policy from 1945 to 1975 failed to bring about full employment. It is known that other countries, such as Sweden, adopted similarly moderate macro-economic policies with an active labour market component, and succeeded in maintaining full employment. Why did Canadian employment policy fail?

A historical analysis illustrates a series of problems that point to three crucial characteristics of Canadian policy. *First*, Canadian employment policy is a responsibility that the federal government has not shared with provincial governments. *Second*, policy has aimed to maximize economic growth rather than employment and higher living standards. *Third*, interest groups have played a marginal role in the elaboration and implementation of employment policies. These characteristics pose a number of problems at the macro-economic level and within the labour market.

Federal Responsibility for Employment Policy

Since 1945, the federal government has held sole responsibility for Canadian employment policy, intervening in three principal sectors — the macro-economic sector, the labour market, and regional economic development. To date, none of the provinces — not even Quebec — has challenged this exclusive responsibility. Federal primacy in this area was achieved by coupling absolute control of relevant national institutions with an ongoing refusal of any provincial participation. The Bank of Canada, the Unemployment Insurance Commission, federal employment and manpower centres, and the ministries of Regional Development and Employment and Immigration, are cases in point.

In an equally direct manner, the federal government has asserted its preeminence in the area of stabilization policy, primarily because it enjoys a much wider margin of financial flexibility than the provinces. This margin is a result of the federal government's exclusive control of the Bank of Canada.

In an earlier era, from 1942 to 1954, the federal government also held exclusive control over the most lucrative taxation categories.[6] And until the current crisis, federal government spending within its areas of jurisdiction has increased at a slower rate than that of the provinces, so that Ottawa has been

able to provide generous financing for programs under joint jurisdiction, such as regional development, as well as programs in areas of exclusive provincial jurisdiction, such as education, health, income assistance and professional training. But the federal government has maintained exclusive control of stabilization policy by demanding equal provincial contributions for shared-cost and joint programs, then scaling down its participation when circumstances improved or when its own financial situation seemed precarious.

Since the Second World War, Ottawa has legitimized its incursions into areas of provincial jurisdiction by claiming responsibility for employment and economic growth, meanwhile equipping itself with the institutional and financial mechanisms it needs to exercise a dominant role in employment policy. This role has never been seriously challenged by Quebec, or by any other provincial government.

At times, particularly in the early 1960s, a deteriorating labour market has led some provinces, notably Quebec, to attempt to stimulate employment. However, with the possible exception of the last few years, policy initiatives by the Quebec government have been sporadic, unsystematic and narrow in scope. In the absence of coordination with the federal government, policies introduced by provincial governments have often duplicated federal programs. Even though employment issues have dominated the political agenda, effective employment policy has not been pursued as a direct economic objective, but rather through an economic development policy designed to produce an acceptable level of employment, which has seldom occurred. Meanwhile, Quebec has not developed a permanent employment strategy, and other provinces seem to be no further ahead. Consequently, instead of a national policy of full employment, there has been a federal approach to employment policy whose failure is apparent, at least in Quebec.

Favouring Economic Growth Over Full Employment

No Canadian government, federal or provincial, has ever expressed a firm political commitment to full employment. Even after the Second World War, when the federal government proposed a Canadian stabilization policy for provincial consideration in the White Paper on Employment and Income, it only signalled its intention to aim for high rates of employment and income.

Economic strategies over the years have given equal consideration to economic growth, price stability, and the equitable distribution of income and employment. In practice, it is clear that employment is often down-played in favour of price stability and economic growth. And in the past decade, some policy-makers have even come to view a policy of full employment as detrimental to economic growth. The Allmand Report, published in 1981, acknowledged and deplored the erosion of the federal commitment to full employment since 1945. The Parliamentary committee concluded that the key to any change in the unemployment situation remained the government's commitment to upholding the concept of "full employment", and generating

the political will to attain this objective. The authors of the report called for the adoption of a national policy on full employment.[7]

Consultation Over Participation

Since the end of the Second World War, at the macro-economic level, in labour market policy and in regional economic development, the federal government has declined to share employment policy-making with strategically important groups or provincial powers. No permanent mechanism has been established to allow for coordination or true participation, and federal institutions have been only slightly regionalized.

At the federal level, strategic economic groups are accorded an essentially consultative role. Various consultative organizations have been established, such as the Economic Council of Canada and the Canadian Employment and Immigration Advisory Council. Various ad hoc committees and commissions have also been created to gather the analyses and opinions of labour, employers and other strategic groups on matters like economic development and conditions of work. One such example in the area of economic development was the Major Projects Task Force, which was established in 1978 and brought together 80 representatives from the business and labour communities. The Task Force was asked to examine the emerging potential of a number of Canadian industrial sectors, and compile an inventory of investment projects that might be under way in each region of Canada by the year 2000.

Among other things, the Task Force recommended the establishment of a tripartite institution which would make decisions, rather than serving in a purely consultative role. The federal government refused to create such an agency, whose role would have been to identify investment projects for government support.

In a recent article, R.J. Adams (1982) analyzed the Canadian government's attitude toward shared decision-making, as opposed to merely consultative participation. He observes that since the Second World War a number of industrial countries have introduced economic decision-making processes that involve the continuing participation of employers and labour. The establishment of such a decision-making process seems to have helped some countries achieve superior economic performance to that of Canada and the United States. Adams evaluates different attempts, beginning in the 1970s, to develop such mechanisms in Canada, initially at the suggestion of the Canadian Labour Congress (CLC), later in response to joint lobbying by the CLC and Canadian business.

In 1976, the CLC manifesto on tripartism recommended the creation of a tripartite social and economic planning council whose decisions would be endorsed by government. In addition, it called for the creation of a tripartite Canadian labour market centre, similar to existing institutions in West Germany and Sweden. This organization would take full responsibility for federal labour market policy, currently administered by the Minister of

Employment and Immigration and th
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The Problems with Federal Employmen

There have been a number of proble
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partite committees to advise on sectoral

Cooperation, the federal government ex-
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t Policy

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y.

The second problem with an exclusively federal, macro-economic policy is that fiscal instruments are shared with the provinces. Since there is no clear division of responsibility, and no coordination of federal and provincial policies, federal initiatives can be neutralized. When the federal government adopts an expansionist policy, the provinces can benefit by improving their budgetary balance, which to some degree wipes out the federal effort.[9] Still, the provinces could be induced to systematically buttress federal policy. A national, rather than a strictly federal, macro-economic policy would provide for coordination of federal and provincial employment policies, while incorporating specific financial measures to enable the provinces to fulfill their responsibilities without being discredited in the financial markets or having to pay higher financing costs.[10]

The third problem for federal policy lies with the choice of expenditures for economic stabilization. Automatic stabilizers such as unemployment insurance and social assistance are highly useful to stabilize income levels, but do not create new employment. They do prevent unemployment from becoming widespread, in sectors of existing production. But automatic stabilizers must be accompanied by non-recurring expenditures more suited to the creation of substitute employment, which can be more easily terminated at the appropriate time. For job creation, the most effective non-recurring expenditures include permanent infrastructure and social capital, both of which fall primarily within provincial or municipal jurisdiction.

This may explain why the federal government has shown a strong preference since 1945 for using social and income security programs to stabilize income. It was easier to take control of these long-standing areas of provincial authority once and for all, than to incur incremental, non-recurring expenses which are necessarily discretionary. It was easier for the federal government to overcome the constitutional obstacles raised by automatic stabilizers than undertake non-recurring expenditures, even though the latter would have been more useful in stabilizing employment.

Federal labour market policy reflects two types of problems: imperfect knowledge about the various Canadian labour markets; and, the very close links between these policies and related provincial initiatives.

In a country the size of Canada, labour market policy cannot operate efficiently unless officials have access to very clear and up-to-date, qualitative and quantitative micro-economic data. Policies must also be sufficiently flexible to reflect regional needs, and changes in those needs over time. Efficient intervention requires a solid understanding and up-to-date information of labour markets in order to identify the needs of the various markets and the appropriate solutions — which often vary from one province to another.[11] Canada's industrial structures vary markedly by region, and geographically within regions. The presence of two national groups with differing institutions and cultures complicates matters further. Faced with several distinct regional labour markets, a unilateral federal policy encounters problems

obtaining and disseminating adequate information about various regional markets, acquiring timely knowledge of problems, developing national solutions that meet the needs of particular regions but can be modified quickly, and creating participatory institutions at the federal level to provide better information and develop more efficient solutions which will be acceptable to strategically important groups.

It is widely agreed that the acceptance of labour market instruments and programs by strategic groups is crucial to their efficiency. In areas like apprenticeship, training, affirmative action, technological change, or work time, government measures will be ineffective if key players have not been involved with the development of solutions, or if they are unwilling to play a communications role and encourage their members to participate fully.

The second problem for federal labour market policy is that the scope of intervention is entirely subject to provincial authority. With its connections to education, labour relations, income security and social policy,[12] and its focus on human resources, labour market policy becomes a bridge between the social and economic spheres.

Over the past 40 years, each new federal labour market intervention has either required a constitutional amendment, as in the adoption of the unemployment insurance program; administrative accommodation, as in professional training programs; or a costly duplication of institutions, as with the Quebec employment centres.[13]

Given the close links between labour markets and other fields of provincial authority, it is extremely difficult for the federal government to develop the range of instruments and flexible measures required to correct structural, regional and demographic deficiencies in the labour market. For example, while most labour market studies recognize the problem of systemic discrimination, the federal government cannot intervene in a comprehensive manner — since labour relations fall within provincial jurisdiction, it cannot establish federal institutions to take an active role in the area. It can act directly with organizations that are subject to federal authority, which represent about 10 per cent of the work force. The same problem arises in areas like technological change and hours of work.

In the 1960s, the federal government entered the field of professional training through administrative agreements with the provinces. Several studies, including the Allmand Report in 1981, acknowledge the mild success of federal policy in this area.[14] The agreements with the provinces are structured around an artificial distinction between education in general and adult training, a distinction which corresponds less and less to reality. The Quebec Commission on Adult Education has recommended that Quebec regain control of professional training, arguing that education policy for Quebec adults cannot be planned without complete control.

In the area of income security, the overlap between federal unemployment insurance programs and jointly funded provincial social assistance poses serious problems of coherence and efficiency. The provinces are not responsible for employment policy or unemployment insurance rules, both of which are modified continually. However, provincial responsibilities are affected by unemployment, through increases in the number of employable social assistance recipients.

To ease their budgetary difficulties, the provinces have tried to develop special measures to facilitate the re-entry of social assistance recipients to the labour market. But due to prolonged periods of unemployment, or lack of work experience, the unemployed who receive social assistance represent the most difficult challenge for labour market re-entry. Moreover, provincial employment programs which only address social assistance recipients appear unjust to other unemployed, especially if they consider themselves poorly served by federal programs.

If responsibility for employment policy is left exclusively to the federal government, a combination of inconsistent initiatives, inefficient programs which are ill-suited to provincial needs, and the duplication of labour market programs serves to discredit all forms of federal or provincial intervention in this area in the eyes of the population. No society can allow such a state of affairs to continue.

DRAWING LESSONS FROM FOREIGN EXPERIENCES

While the Canadian economy has not performed successfully over the past 15 years, other countries — particularly Sweden, Norway and Austria (see Table 1) — experienced relatively low levels of unemployment through the 1970s. The well known successes of the West German economy petered out in the early 1980s, but it is interesting to study this decline.

We do not propose to describe the economic policy adopted by each of these countries since 1975 in great detail. But briefly, Austria's success reflects an astute combination of primarily macro-economic instruments, including budgetary, monetary, exchange rate and income policies. In Norway, full employment was brought about by a series of expansionary budgets, financed directly by revenues from the petroleum sector, although it recently became necessary to combine this macro-economic policy with a selective employment strategy. The Swedish government pursues full employment as a matter of course, through an active labour market policy. West Germany's lacklustre performance in recent years can be explained by its adoption of restrictive macro-economic measures. The following conclusions, drawn from the detailed analysis carried out in *Le défi du plein emploi: un nouveau regard économique*, reflect the four conditions which we believe were integral to the success of European full employment strategy.[15]

Table 1

Unemployment Rates Standardized by the O.E.C.D.
Selected Years

	1968	1970	1972	1974	1976	1978	1980	1981	1982	1983	1984
First Group											
West Germany	1.5	0.8	0.8	1.6	3.7	3.5	3.0	4.4	6.1	7.5	7.3
Austria	2.0	1.4	1.2	1.4	1.8	2.1	1.9	2.5	3.5	4.2	—
Norway	2.1	1.6	1.7	1.5	1.8	1.8	1.7	2.0	2.6	3.1	3.2
Sweden	2.2	1.5	2.7	2.0	1.6	2.2	2.0	2.5	2.5	2.5	3.2
Second Group											
Canada	4.4	5.6	6.2	5.3	7.1	8.3	7.4	7.5	10.9	11.8	11.3
Québec*	5.6	7.0	7.5	6.6	8.7	10.9	9.9	10.4	13.8	13.9	12.8

Sources: *Statistics Canada. *The Active Population; Chronological Statistics on the Active Population.*

OECD. *Economic Overview of the O.E.C.D.*, Paris, July 1984.

Employment-Centred Strategies

An analysis of the economic policies adopted in each of the four countries demonstrates there is no single way to achieve and maintain full employment. Each country has its own model, and each has occasionally reformulated its models. Thus, Sweden's Rehn-Meidner model is different from the Swedish model in the post-war period, and it is likely that the model for the year 2000 will be quite different from what we are familiar with today.[16]

The institutions of each country have been shaped in conformity with economic history and culture. For example, the specific structure of the Austrian economy necessitates a strong currency, so that its economic strategy cannot incorporate currency devaluation, as does Sweden's. Whereas the Austrian and Norwegian models are based largely on macroeconomic policy (taxation, transfers, interest and exchange rates), Sweden relies primarily on labour market policy. These differences probably reflect the fact that Austria has established a rigorous incomes policy, while Norway, benefitting from petroleum revenues, is able to combine its fiscal and income policies. Though existing Swedish institutions allow for some central negotiation over incomes, it is not possible to have an incomes policy as strict as Austria's, so Sweden has substituted labour market policy for macroeconomic measures.[17]

It is possible, perhaps likely, that the Austrian and Norwegian models will be transformed, assigning a more active role to labour market policy in the future. But even if this takes place, it cannot be assumed that Austria and Norway will copy the pre-1950s Swedish model. In some respects, the Austrian and Norwegian models are as different from each other as they are from the Swedish model.

As in Sweden, past West German strategy has centred on labour market policy. However, this policy is very different from its Swedish counterpart. Whereas Swedish labour market programs and measures aim to stimulate demand for jobs, West Germany focusses principally on job supply. It appears that no country can be said to have simply imported a model from elsewhere.

However, notwithstanding the apparent differences among specific policies, there are numerous similarities in general policy orientation. First and foremost, the countries which have achieved full employment have made it their first objective. We will return to this crucial point in a moment.

Second, the full employment countries hold similar attitudes with respect to public spending deficits. This is not to say that they pursue full employment simply by accumulating budgetary deficits. On the contrary, each country is concerned in its own manner with deficit control, and with sound management of the national debt. Norway is perhaps the only country to pay less attention to its deficit, since the Norwegian public sector, drawing on petroleum revenues, operates with a financial surplus. Austria, by contrast, is concerned with the extent of a deficit which, in comparison with other OECD countries, is far from alarming. While it appears difficult to justify this concern, Austria's efforts to contain its deficit are commendable. Unlike West Germany and Canada, Austria does not control its debt by reducing social spending, but uses appropriate fiscal measures in conjunction with employment policy. Both taxation and employment have the capacity to increase revenues. By contrast, cuts in public spending contribute to greater unemployment and thus reduce taxation revenues, causing further deficit increases. This is illustrated dramatically in both West Germany and Canada.

The third striking difference concerns the use of economic policy to fight inflation. Like everyone else, the full employment countries are concerned about inflation. But in contrast to recent Canadian policy, they have not adopted policies that increased unemployment to fight the scourge of inflation. Rather than presuming an inevitable choice between inflation and unemployment, they recognize that exclusive reliance on macro-economic policy to attain full employment can create inflationary pressures. Far from being compromised, their objective of realizing both full employment and price stability is attained by combining macro-economic measures with other policies, such as a strong currency matched with negotiated incomes in Austria, or an incomes policy based on fiscal management and a policy of credit in

Norway. In Sweden, inflationary pressures are avoided by using labour market policy to bring about full employment.

Income policies in these countries are hardly similar to the practice of wage controls in Canada. Wage increases are settled through a dual process which assigns an important role to centralized negotiations. If unions consider the economy's overall health and not just that of a particular company during wage negotiations, it is because unions influence the direction of general economic policy, and are convinced that full employment is an over-riding objective. Union cooperation in the overall battle against inflation reflects the orientation of economic policy towards full employment.

Conditions For A Successful Full Employment Strategy

Although full employment policy in each country is based on a markedly different model, they all have points in common which can account for their success. In this regard, West Germany's failure makes it possible to assess whether the common points which we consider necessary conditions for achieving full employment are fully justified. The four conditions are a political commitment to full employment, the participation of social partners in policy formulation, and an institutional commitment to bring about both full employment and administrative decentralization.

The political commitment of government and social partners to full employment is basic to the success of a full employment strategy. In other words, full employment must be the chief objective for a society that wishes to embrace a full employment strategy. This political commitment on the part of all participants must translate into behaviour that recognizes the irrationality of social, political and economic programs which adopt a passive attitude towards unemployment.

This first condition for success is not merely verbal. It is not enough that governments, unions, employer's associations, and other groups confirm that they hold full employment as an over-riding priority. Their policies, programs, attitudes and behaviour must incorporate their political commitment to full employment.

For governments, this commitment is reflected in choices which take specific account of the employment problem, so that employment becomes a criterion for decision making.[18] In countries with full employment policies, corporate subsidies often take specific account of employment impact, and the criteria of employment becomes an important consideration in the development of specific policies and regulations. Assigning higher priority to employment also requires unions and employers to modify aspects of their behaviour, to consider the impact of wage and price negotiations on employment. Even faced with layoffs, employers may be more inclined to maintain employment levels.

This commitment is at the heart of what Austria, Norway and Sweden have achieved. In West Germany, as in Canada, it is claimed that full employment is being pursued. But in the West German and Canadian strategies, full employment would instead be the consequence of pursuing other objectives, such as deficit reduction, stimulation of private investment, or free trade, so that full employment is seen as a fortunate consequence and not as an immediate objective.

It might be suggested that this first condition would require so profound a transformation of mentalities, attitudes, and political will that it would be impossible to achieve given current social conditions. It is true that the acceptance of such an objective does not just happen. In each of the full employment countries, it is the union movement that has sold the population on the objective, with the help and support of a political party. Once the strategy is entrenched, the parties in power may change, but a full employment policy is maintained as long as the union movement participates in the formulation of economic policy. This role is the second condition for success.

The role of concerned groups, especially unions and employers associations, includes participation alongside governments in the formulation of policies and the choice of specific programs and measures. This participation is essential to ensuring that full employment continues to receive high priority over time. In West Germany, when the unions withdrew from "Concerted Action", the government watered down its commitment to full employment and the battle against inflation and the government deficit gradually became the political priorities.

But participation is also necessary to ensure the effectiveness of the measures and policies adopted. The achievement of full employment under conditions of relative price stability cannot rely on the unilateral behaviour of one economic actor. It is futile to expect that the government could act by itself to bring about full employment, with economic consequences acceptable to all. Government-established interest rates or budgetary and fiscal policy can increase aggregate demand in order to create enough employment to absorb surplus labour. But within the framework of existing institutions, inflationary pressures could develop.

For precisely this reason, in all the countries studied, macro-economic policy is accompanied by complimentary measures. The government can also assume the responsibility of being an employer of last resort. But without the participation of concerned economic groups, it is unlikely that the jobs thus created would ideally suit the needs of the target population. Nor can unions or employer associations act unilaterally to create full employment. The wage concessions that many employers have demanded from unions do not generate full employment — on the contrary, they can bring about a drop in employment due to a decline in consumption. The logic of the market prohibits businesses from investing or hiring workers when it is not profitable to do so. In spite of moral and other pleas, the private sector cannot be

expected to increase investment and hiring to the point of full employment. In today's industrial society, variations in production levels, employment and prices are the result of the interdependent actions of different groups.

The participation we propose is more than mere consultation. It is a serious mistake to assume that measures adopted by government following consultations with unions and employers are defined by the consulted parties. Rarely do these groups express the same views to government on a particular issue. On the contrary, in a consultative process, it is normal for each group to advance the position which it considers most advantageous over the short term. Since unions and employers normally express opposing views, the mediation carried out by government cannot be identified as the choice of the participants.

Nor is it necessary to cast this participation as dialogue in the traditional sense of the term, leading to the establishment of consensus. Indeed, it would be utopian to expect North American unions, employers and other groups to concur on joint economic actions. Homogeneous groups, free of major conflict, can consult together and reach consensus. But when the nature of the participants suggests potential for major disagreement, participation becomes a process of negotiation. Within the framework of a full employment strategy, the negotiations must enable the groups to specify the most appropriate measures and programs for attaining full employment.

Yet participation in the pursuit of full employment cannot be reduced to negotiations, either within companies or in the larger framework of a particular industrial sector. Companies and sectors are too limited as entities to adopt efficient measures and programs, and since not all companies and sectors are unionized, the participation of groups limited to certain sectors risks marginalization of non-unionized sectors. To adopt effective measures and avoid ghettoizing some sectors, concerned groups must be prepared to participate on a social or collective scale.

It is obvious that the process of negotiation requires workers and employers to come together in a framework. High rates of unionization are not at all alien to a successful process of negotiation, but the social partners must agree to confer with each other — they cannot be obliged to do so. The spirit of cooperation arose voluntarily in each of the four countries studied, although it is true that the governments of the day often held a favourable bias towards labour, which encouraged employers to seek agreement with the union movement in order to ensure economic growth. The negotiation process will also fail if there is no consensus of values between the parties, or if analyses of economic conditions and current economic problems seriously differ. For this reason, Austria and Norway each established a technical council with expert representation from employers and the union movement.

The third condition for success is institutional commitment. It is not enough for various economic groups to give priority to full employment, then modify their behaviour and participate in the development of measures and

programs. The conditions for success must still be incorporated in a new institutional framework, with a mandate to ensure that the strategy is firmly founded. These institutions ensure the continuity of the strategy, and monitor the consistency of the various measures adopted.

The institutional framework for a full employment strategy varies from one country to another. It is defined according to the particular culture, history, society, economy and politics of each country. It is precisely because of these individual factors that a country can choose the institutional development of one sector at a particular point in time over another. For example, Sweden chose to rapidly institutionalize the labour market sector, while Austria developed an institution to negotiate the general direction of economic policy.

The decentralization of administrative and decision-making processes within a federal structure is the fourth condition of a successful full employment strategy. It is essential as a means of ensuring efficient labour market and regional economic development measures. To anticipate the development of regional unemployment, and to solve chronic unemployment for particular groups and regions, *measures and programs must be based on current and correct information*, through a decentralized institutional and decision-making structure. As noted above, the opposite situation now prevails in Canada.

Information is less of a problem when decision-making is decentralized and concerned groups participate in the decisions. When the pertinent information is available to the people who must make the decisions, action can be taken when problems are first identified.

But decentralization is just as important as a catalyst to make local groups more responsible, which contributes to the effectiveness of full employment measures. Since relations are more personal at the local level, and each group is familiar with its own milieu, administrative decentralization is more likely than central organization to augment the multiplier effects of various employment measures. Because local groups are better able to perceive the economic advantages of full employment, they become less prone to partisan and ideological conflict. This is why West German tripartism continues to operate in the framework of labour market policy, even though it broke off at the central level nearly 10 years ago. At the regional level, the parties have a greater understanding of the importance of full employment to economic success. Thus, decentralization ensures political stability for the full employment strategy, by placing it above and beyond political wrangling.

Decentralization does not remove all responsibility from the national level. National authorities must define priorities, and resolve potential conflicts between various regions and sectors. They also have a role to play in ensuring that minimum standards are respected. Finally, the national structure must define macro-economic policy and establish the main lines of development.

In short, a full employment strategy constitutes a complex challenge. Every country possesses the ingredients to produce full employment. But to realize

full employment in an efficient and equitable manner, it is necessary to heed several rules or conditions of success, including political commitment, participation, decentralization and institutional commitment.

THEORETICAL FOUNDATIONS OF A FULL EMPLOYMENT STRATEGY

The four conditions for success can also be deduced from theoretical analysis. We will demonstrate as succinctly as possible how these conditions are logically derived from the addition of four basic hypotheses to the foundation of a Keynesian model.

The first hypothesis concerns individual behaviour. In our view, contemporary economic reality is more complex than it was some centuries ago. From this perspective it is inadequate, and indeed wrong, to attempt to explain all human behaviour on the economic level by assuming that the rational individual aims solely to acquire maximum wealth with the least effort. It remains legitimate to assume that, on the economic level, all individuals follow their personal interest. But this personal interest can acquire a modern form which surpasses the pursuit of maximum monetary gain.

We do assume that each individual whose behaviour is economically rational will always prefer, everything else being equal, to have more income rather than less. But we want to put forward the supplementary hypothesis that each individual in modern society aspires to economic autonomy and seeks economic security. This motivation leads the individual to simultaneously seek both a higher and a more stable income, but these two objectives are sometimes contradictory: a higher income can prove to be less stable. Because the large majority of people prefer to avoid risk, they will usually accept a lower income which is more stable.

This hypothesis is corroborated by numerous examples, the most obvious of which is public behaviour concerning commercial insurance. In effect, people will buy insurance policies even if the premium is much higher than the mathematical expectancy of loss. The need for economic security thus constitutes the primary force behind economic motivation.[19]

We will return to the consequences of economic behaviour dominated by the need for economic security. For now, it is enough to see the modern phenomenon which is reflected in this hypothesis. Lester C. Thurow writes:

> Economic security is to modern man what a castle and a moat were to medieval man. One would have expected that the desire for economic security would fall as the danger of real starvation and exposure faded into the past. But this hasn't happened. Instead, the desire for economic security is probably the major economic demand confronting the political marketplace. Everyone wants economic security and government is seen as the prime vehicle for guaranteeing it. The drive for economic security dominates our actions, and may end up dominating our economy. (1981, p. 19)

The second hypothesis concerns the significance that each individual attaches to holding paid employment. According to this hypothesis, *the wage system is the distributive mechanism for incomes favoured by modern industrial society.* If individuals aspire to economic autonomy and security, they in fact aspire to receiving a decent and stable salary and therefore to engage, as long as they wish, in paid employment.

Some might think that having an income is enough to establish economic independence. We do not dispute that some high incomes obtained through inheritance or the lottery make some people independently wealthy. However, while very few people win a lottery or are born into a rich family, everybody aspires to economic autonomy. In other words, the vast majority prefers to receive income from employment rather than from income transfer programs.

At one time, and this includes the whole period of industrialization, human work was indispensible to survival. Hard work was just about the only way of providing for one's economic autonomy. In several countries, this is still true. However, in Canada as well as other industrialized countries, machines, electronic intelligence and robots are capable of replacing many hours of human labour. The current problem is not a lack of workers, but a lack of employment. Because human labour is no longer indispensible to the production of goods necessary for economic independence, it has been argued that collective values will change, and in particular, that the value attributed to work will disappear. Collectively, we will then be able to ensure each individual's economic autonomy by allocating incomes, or the fruits of robotic production, through income security measures such as a guaranteed minimum income. Those who do not have access to employment would thereby be guaranteed this income, and unemployment would no longer be a problem.

But in current industrial societies, *property contracts are defined* in such a way that we cannot think of redistributing incomes in a manner that gives each group of recipients a feeling of independence. Earned income accrues only to those who obtain it by hiring out their labour power, or by utilizing their physical or financial capital. And we only think of income from work and property as *earned*, that is to say *deserved.*

Other forms of income are subject to more or less precarious family agreements, gifts or charity. Yet because they do not properly belong to those who receive them, such incomes cannot give their recipients economic independence. Since incomes distributed in the form of an allowance, a gift or as charity can be cut off from one day to the next, at the pleasure of the so-called true owners, they offer no economic security.

From this perspective, an income cannot ensure economic autonomy and security unless it is earned. For the majority of people, this means receiving a wage in exchange for work performed in a job. So in the context of current

ownership contracts, society is unable to ensure economic autonomy for all, except by offering each individual the possibility of being employed.

The situation of women is interesting in this regard. Throughout the process of industrialization, and until just recently, there were many women who did not participate in the labour market. Women were almost exclusively occupied with housework; though generally unpaid, this work gave rise to an implicit redistribution of monetary income on the part of the spouse who participated in the labour market. For a long time, women felt secure with this informal family agreement: the bonds of marriage were more stable than they are today, and any monetary surplus beyond the sums required to satisfy basic needs was generally small. In recent years, however, divorce rates have increased and women have rapidly realized that they must be able to engage in paid employment if they do not want to fall into the poverty which is their destiny under social assistance.[20]

The third hypothesis concerns market imperfections. First, just as some Keynesians have incorporated the work of institutional economists on the structure of markets, we recognize that private enterprises do not operate in an environment of pure and perfect competition. The operation of private enterprises in an environment of imperfect competition merits more exhaustive treatment than is allowed here. However, we want to focus on one of the fundamental characteristics of imperfect competition, which is the possibility of companies acting in concert to influence prices. In effect, since the number of companies serving a market is relatively limited under imperfect competition, it is possible and advantageous for them to join together in the hope of controlling the market and obtaining favourable government regulations.

The second factor relating to market imperfections concerns mobility problems. We attach significance to the hypothesis that the perfect mobility of goods and services, and of human and physical resources, runs up against numerous obstacles. Instantaneous occupational mobility cannot occur given the time required for appropriate training; labour is not completely mobile from one region to another, and the mobility of markets is limited by regulations governing zones, prices and wages, tariffs and other requirements of international trade.

Those who extol the growth of market competition believe that, if prices and wages were more flexible and there were no regulatory obstacles to the mobility of goods, services, capital and manpower, new economic development would reduce regional inequities, gaps in income, and industrial bottlenecks arising from scarcities of resources, manufactured goods and specialized manpower. In this view, price rigidity combines with barriers to mobility to generate inflationary pressures before full employment can be reached. In order to attenuate these market imperfections, regulations detrimental to mobility and price flexibility should be abolished, and programs should be initiated to support manpower training and reduce relocation costs.

These recommendations are included in the report of the Royal Commission on the Economic Union and Development Prospects for Canada. In themselves, they may not be all bad, but they appear insufficient to ensure full employment. Among other things, it seems utopian to think that capital and human resources are primarily subject to the impetus of prices and that structural problems will be ironed out by themselves because there is more mobility of goods, services, capital and manpower. In reality, while people are generally sensitive to monetary incentives, they are equally subject to other factors such as tastes, values, prejudices, and tradition, which can sometimes prove more powerful. This approach also fails to consider the economic logic of various regulations, which would be politically difficult to abolish without alternative solutions. We will return to this in our discussion of the fourth hypothesis.

A third factor concerns market imperfections and the pursuit of economic objectives in the national interest: the choice of market forces versus national intervention. The current status of Canada's transportation and communications systems, as well as technological imperatives that favour large-scale production, dictate that the territory over which a market can extend may exceed national geographic boundaries. Thus, the logic of market development does not necessarily correspond to the logic of industrial development on the national level. Moreover, considering that the owners of key companies are not always citizens of the country in which they operate, there is less reason to presume that corporate development will necessarily conform with national economic development objectives.[21] This hypothesis is important, because it explains why economic development left entirely to market forces can create economic dislocations, and do so on a proportionally larger scale in a small country.

The fourth hypothesis concerns the presence of interest groups.[22] Markets are sometimes unable to satisfy every need, and public administrations sometimes have difficulty identifying the needs to which they should respond. In this context, interest groups are formed to meet needs which cannot be satisfied by either governments or markets.

An interest group is generally defined as "a certain number of individuals linked by a common interest" (Olson, M., 1978, p. 28). On this basis, not all interest groups are necessarily structured in organizations. Nevertheless, in our societies, there are a multitude of organized interest groups, including unions, employer associations, professional organizations, fraternal orders, agricultural cooperatives, consumer associations, friendship associations, feminist groups, pensioners' associations, and neighbourhood organizations.

On the economic level, some groups are obviously more important than others. Employer associations and unions can exercise greater economic influence than friendship associations or neighbourhood organizations. Yet, by definition, individuals belong to a group with the hope of benefitting, if not financially, then from the goods and services the organization is able to offer.

In fact, many needs are not satisfied by markets because the required goods and services are not divisible into appropriate units, could prove difficult to market, or are not easily and economically accessible. These goods and services are called public goods, and can often be produced by interest groups.

Interest groups can be categorized as producers of public goods and services, or as advocates for the protection and improvement of their members' income. The latter function also incorporates an element of public good, since the improvement of a specific group's income benefits all members of the group, regardless of each individual's contribution to the collective action. These strategic groups, as we have called them, generally seek two things: economic security, and a better standard of living. Unions and employer associations belong to this category, and the pursuit of these two objectives structures their collective actions.[23]

The Pursuit of Full Employment: A Fair and Effective Strategy

From the four hypotheses developed above, we can deduce several observations about the operation of the economy. In this account, we will discuss two of these observations.

The first observation is that the economic organization which ensues from an imperfectly competitive market economy based on laissez-faire thinking is inefficient, in that it is possible in such an economy to increase the production of one good without diminishing the production of another good. This is due primarily to the existence of strategic groups.

Strategic groups themselves are clearly not the source of inefficiency, but the instruments which develop in response to the functioning of the economic system. But the rationale under which they operate, developed in a context of competition, is at the root of the problem.

There are two ways for a strategic group to attain its objectives. It can seek to improve and safeguard the income of its members by working to increase and stabilize national income, but it cannot do so alone. A national effort to improve and stabilize income requires the participation of these interdependent economic groups. To adopt this strategy, a group must negotiate with the other groups with which it interacts.

A strategic group might also seek to increase its share of the national income through restrictive or protectionist measures. If it succeeds in neutralizing would-be competition by exercising strategic power or having legislation enacted, it does not require the participation of other groups.

These strategies are very different, in approach and in their social consequences. The first strategy serves the interest of society as a whole, since it aims to meet each group's objectives by increasing the size of the economic pie. The second strategy, on the other hand, serves one group's interest by reducing the share of the pie remaining for others, and may even diminish the size of the pie.[24]

In a society that favours competitiveness and competition between individuals and groups, and refuses to encourage social negotiation, small strategic groups will naturally arise through the will of their members. But because they are in competition with others, and cannot negotiate with non-existent larger groups, their only strategy is to increase their share of national income through protectionist measures. To illustrate, any domestic industry whose existence is threatened by the low price of competitive imports can attempt to increase productivity, reorient surplus human and physical resources towards sectors where they are more competitive, or bring pressure to bear on elected representatives to adopt protectionist tariff measures. The first solution is more advantageous to society than the second, but it is not at all clear that it will be endorsed in an individualistic society. The redeployment of surplus human and physical resources essentially requires that agreements be concluded with other groups, whose support for this strategy is required, but larger groups of this sort often do not even exist. In other words, this strategy could only be adopted if the society developed institutions that favoured mediation and social negotiation, or if all economic actors were driven towards a shared objective such as victory in wartime, or full employment.

Without such a common goal, companies and workers could very well oppose the strategy rather than accepting redeployment. Workers and employers might join together to demand protectionist tariffs. Without participation or negotiation on a national scale, this strategy is the only rational one for a small strategic group acting alone. But society would be better served by measures that improve international trade, while ensuring the economic security and productive utilization of the human resources that would need to be integrated into new tasks.

This idea is developed, albeit differently, by both Olson (1978, 1983) and Thurow (1981). In a society that always favours competition and individualism over social negotiation, only small strategic groups will be created, and protectionism will generally be the only strategy they can adopt to achieve their ends. This is better than unmitigated "laissez faire", but less welcome from the perspective of social efficiency than wider social negotiation.[25] This is further demonstrated by an analysis of the three principal avenues open to strategic groups for achieving their goals in a market economy.

The first avenue available to some strategic groups is to use the powers assumed by cartels. The strategic group, comprised of the key firms in an industry, wields its market power to extort monopoly-level profits. Economic theory, based on long study of the consequences of cartel arrangements, concludes that cartels harm the social system by producing smaller quantities of goods than the society requires and selling their production at a higher price.

The second avenue available to strategic groups, negotiation, is of special interest to unions. Unlike cartels, unions are not able to act unilaterally to improve and protect their income. Since they only represent salaried workers

and do not own the companies they work for, unions must seek to conclude agreements on work conditions with their employers. In Quebec and Canada, union negotiations take place primarily at the company level. While some sectoral negotiations do occur in construction, railways and the public sector, or when collective agreements are extended by decree to an entire sector, this wider forum is relatively limited compared to the importance that it has assumed in countries like Sweden, Norway and Austria. Contrary to the practice in these countries, sectoral negotiations of a collective nature are not really encouraged in North America. Bargaining is aimed at concluding agreements over work conditions within a company, and is not concerned with general economic policy.

But if small-scale negotiations in the workplace succeed in improving the economic positions of the parties, they are of much less benefit to non-unionized workers. Most often, negotiations protect the short-term interests of members covered by the agreement. However, if negotiations were extended beyond wages and work conditions to economic policy, and covered a larger field than the company or sector, it is possible that the benefits would also extend beyond the union movement. Unfortunately, since negotiations in North America are limited in scope, they sometimes result in the adoption of clauses and practices judged protectionist or unproductive by non-unionized workers. But the parties to the negotiations are not to blame. They act rationally, given the conditions of the economic system within which they operate.

The third avenue for strategic groups, which is widely used in Canada, Quebec and in North America generally, is legislative action. Political lobbying is a substitute for social negotiations, so the most frequent method of intervention for strategic groups is the use of pressure tactics to persuade governments to adopt legislation or regulations which protect and support their income. Not all laws and regulations are strictly the result of interventions by strategic groups. Governments are called upon to regulate different sectors of the economy, when competition and markets do not bring about expected results. But many regulations, including work standards, prices and quotas in the agricultural sector, regulation of transportation, customs duties to protect certain industries, and entry limits in various professions, result from pressures exerted on governments by interested groups.

Given the extent of this sort of legislation and regulation, it cannot be considered that the intervention of strategic groups is of marginal importance. In the current context of North American institutions, lobbying is just about the only means of ensuring economic security.

It bears repeating that legislative action is a substitute for social negotiation. For example, the minimum wage does not exist in Sweden because 80% of workers are unionized and have the instruments to negotiate work conditions. Even if legislative activity takes place in response to real problems,

these problems may also be resolved in a manner that is sometimes more socially effective.

It is unfortunate that recourse to legislation is one of the only avenues for strategic groups in Quebec and Canada to obtain certain objectives. If we wish to have better and perhaps fewer laws and regulations, we must find another way for strategic groups to gain the economic security they seek.

We have suggested that a social system based on competition and organized into strategic groups gives rise to an inefficient economic system. This social system leads to a less than zero-sum game, where uncoordinated actions produce losses for society as a whole.[26] We would argue, further, *that full employment is a necessary condition for the efficient organization of production, and that full employment is a public good which cannot be achieved spontaneously.*

The first part of this proposition is easily understood. By definition, an economy is efficient when it is impossible to increase the production of a good without having to diminish the production of another good. But when human and physical resources are under-utilized, it is always possible to increase the production of one good without cutting back on another. Since an economic system is only efficient to the extent that it fully utilizes available resources, full employment is a necessary condition of efficiency. But it is not the only condition, in that not every full employment economy is necessarily efficient.

The second part of the proposition is somewhat more abstract. Based on our hypotheses, especially concerning strategic groups and market imperfections, it follows that an efficient, full employment economy is a public good because *full employment is beneficial to all groups, even though it cannot come about through the spontaneous action of those groups.* The benefits of full employment, like any other public good, accrue to all groups, and it is difficult to exclude groups that have not contributed. But because there is considerable interdependence among groups, efficient full employment cannot be achieved by the unilateral action of any one of them. *Efficient full employment is the result of interdependent actions on the part of all strategic groups. But to achieve it, each group must be persuaded to modify its economic objectives.*

The pursuit of full employment means that strategic groups must adjust their behaviour to seek the maximization of national income under full employment, rather than the maximization of their part of the pie. Yet these changes cannot come about spontaneously. Oligopolistic companies and unions will not modify their behaviour if they are not certain that other groups will do the same. *The pursuit of efficient full employment must, therefore, be an over-riding social objective to which all groups conform.* It falls to the state to see that this commitment is made.

To make full employment its first objective, a government must develop a strategy that recognizes full employment as a public good. First, it must make full employment its over-riding policy objective, so that employment,

rather than growth or value added in production, becomes the leading motivator of its actions. In order to ensure the participation of relevant strategic groups, this objective must be forcefully proclaimed. An effective full employment strategy requires the elaboration of macro-economic policies and measures, including components that affect the labour market and regional economic development, through a process of negotiation among the strategic groups concerned. This process of social negotiation guarantees that economic growth will be maximized within the constraint of achieving full employment. It may also be necessary for strategic groups to participate in the administration of measures affecting the labour market and regional economic development. Such democracy at the administrative level will ensure the effectiveness of the various elements of the program.

It goes without saying that this process must be organized in a clearly-defined institutional context. This is the only way for government to ensure permanent, continuing priority for the pursuit of full employment. This institutional commitment must take the form of an institutional network, in which local and regional ramifications are accorded an important role in administration and decision-making.

Although full employment is essentially a public good which results from the interdependent actions of groups, national authorities cannot plan the desired behaviour of agents at the local level. Local and regional authorities, including concerned strategic groups, are in a much better position to act — they are to the achievement of full employment what individual markets are to the production of private goods. Ultimately, the four necessary conditions we have identified for a successful full employment strategy also follow from the addition of theoretical hypotheses to the Keynesian model. They allow us to identify the characteristics of an interventionist strategy which can sustain full employment, and is more equitable and efficient than a strategy directed towards increased market competition.

It must be emphasized that the introduction of such a full employment strategy can encounter many obstacles at the political level. The theoretical recognition of the good derived from such a strategy is not sufficient to guarantee its adoption. This strategy is almost synonymous with greater democracy, since it requires the sharing of political power, but power is perhaps a difficult commodity to share spontaneously. This is why government must play a key leadership role, by clearly expressing its unswerving determination to achieve full employment. This is one of the only ways for the government to persuade strategic groups such as employer associations, for which employment is not a priority, to participate in negotiations over the appropriate measures to achieve the overall objective.

In conclusion, it is worthwhile to clearly state the common elements which emerge from the historical, comparative and theoretical analyses of the full employment question. These common points reflect the challenges that a society must meet in order to achieve full employment.

First, it is clear that full employment is more than a commendable social objective. It is a key factor in the attainment of such objectives as efficiency, equity and stabilization — it is, in fact, the necessary condition for reaching these objectives. The pursuit of full employment ensures that, even when a society prizes efficiency, the losers will be compensated. Employment generates an allocation of incomes which satisfies the important social values embodied in the work ethic. And finally, full employment serves to stabilize employment and prices all at once. *In other words, the pursuit of full employment becomes the invisible hand.*

Second, the effectiveness of most policies depends largely on the participation of concerned strategic groups. Policies to promote efficiency, equity, and the stabilization of employment and prices cannot be imposed; they must be accepted by the strategic groups, since each group can impair the proposed objective by using its power within an interdependent economic system.

Nevertheless, in industrial societies like Canada and Quebec, this participation can only occur through collective negotiations. *The quest for a mutually advantageous agreement allows strategic groups with divergent interests to participate in a full employment strategy.* The pursuit of efficiency, equity, and price and employment stabilization requires that society acknowledge the existence of strategic groups and further their institutionalization, rather than seeking their destruction.

Third, analysis demonstrates the need for stable institutions to ensure the continuity of policy. Society cannot become efficient and equitable and seek to stabilize employment and prices, once and for all. On the contrary, the pursuit of these objectives requires continuing policy intervention to reflect changing circumstances.

Finally, decentralized decision-making appears to be necessary to ensure the efficiency of some policies, notably economic development and labour market policies. In each case, the knowledge and participation required are of a strictly local or regional nature. Institutions responsible for the administration of these policies must reflect this need.

NOTES

1. D. Drache and D. Cameron, eds., *The Other Macdonald Report* (Toronto: James Lorimer and Company, 1985).
2. Government of Canada, Minister of Reconstruction, *Employment and Income* (Ottawa: 1945).
3. _____, Dominion-Provincial Conference on Reconstruction, *Proposals of Government of Canada* (Ottawa: 1945).

4. On this subject, see D. Bellemare, *La sécurité du revenu au Canada : une analyse économique de l'avènement de l'Etat-Providence*, Ph. D. thesis (Montréal: McGill University, 1981).

5. In this regard, see H.S. Gordon, *A Twenty Year Perspective: Some Reflexions on the Keynesian Revolution in Canada*; and J.J. Deutsch, *Canadian Economic Policy 1945-1965, A Summing Up* (Canadian Trade Committee, 1965); T.N. Brewis, *Canadian Economic Policy* (Toronto: McMillan, 1965); and L.H. Officer and B.L. Smith, *Stabilization Policy in the Postwar Period* (Toronto: McGraw-Hill, 1970).

6. See J.C. Strick, *Canadian Public Finance* (Toronto: Holt, Rinehart and Winston of Canada, 1973).

7. Cf. Government of Canada, *Du travail pour demain : les perspectives d'emploi pour les années 80*, Rapport du Groupe de travail parlementaire sur les perspectives d'emploi (Ottawa: 1981).

8. R. Lacroix and Y. Rabeau, *Politiques nationales, conjonctures régionales : La stabilisation économique* (Montréal : Les Presses de l'université de Montréal, 1981).

9. On this subject, see C. Barber and J. McCallum, *Unemployment and Inflation* (Toronto: James Lorimer and Company, 1980).

10. R. Lacroix and Y. Rabeau, *Propositions pour une politique de stabilisation économique régionale du Canada*, Cahier no. 7934, Département de sciences économiques et Centre de recherches en développement économique (Montréal : University of Montreal, 1979).

11. See N.M. Meltz, "Manpower Policy: Nature, Objectives, Perspectives," in *Manpower Planning for Canadians: An Anthology*, Lerry F. Moore, ed. (1975).

12. Government of Quebec, *Pour une politique québécoise de main-d'oeuvre*, unpublished draft white paper (Québec : Ministère du travail du Québec, 1971).

13. See B. Goldman, *New Directions for Manpower Policy* (Montreal: C.D. Howe Research Institute, 1976).

14. Government of Canada, *Du travail pour demain*.

15. This study was based on an analysis of OECD studies and other documents, as well as a series of interviews with employers and union and government officials responsible for labour market policy in each of the countries. The interviews were undertaken in 1983 with the financial assistance of the National Productivity Institute.

16. See E. Lundberg, "The Rise and Fall of the Swedish Model," in *Journal of Economic Literature*, March, 1985.

17. G. Rehn, "La politique du marché du travail en Suède : le lieu d'une coopération entre le gouvernement et les partenaires sociaux," in *Les stratégies de reprise, Actes du 3ième colloque de l'Association d'Economie Politique*, D. Bellemare and C. Saint-Pierre, eds. (Montréal : Editions Saint-Martin, 1985).

18. For a discussion of the possible conflicts between maximizing production and employment see F. Stewart and P.P. Streeten, "Conflicts Between Output and Employment Objectives," in *Prospects for Employment Opportunities in the 1970s*, R. Robinson and P. Johnston, eds. (HMSO, 1972).

19. Individual behaviour with respect to risks, insurance, and lotteries has been studied by a number of economists. Published works include F. Knight, *Risk, Uncertainty and Profit* (London: Percy Lund Humphries and Co. Ltd., 1933), and Friedman and Savage, "The Utility Analysis of Choices Involving Risks," in *Journal of Political Economy*, August, 1948. The literature shows that individuals will pay high premiums to avoid costly risks whose probability is small, but that at the same time, they are willing to pay for a minute chance of increasing their income. This paradox does not contradict the hypothesis that people can seek economic security, while giving up a small amount of money to treat themselves to a moment of illusion. This is also the reason that social assistance recipients will often turn down minimum wage employment, preferring the stability of social assistance benefits. From this perspective, measures to ensure employment stability also serve to encourage labour force participattion.

20. D. Bellemare, G. Dussault and L. Poulin Simon, "Les femmes et l'économie," in *La Commission sur l'égalité en matière d'emploi* (Ottawa: 1985).

21. See, among others, Gay, *Ce que vous coûtent les investissements étrangers* (Montréal : Leméac-Le Devoir, 1971); K. Levitt, *La capitulation tranquille* (Montréal : Réédition-Québec, 1972); and P. Phillips, *Regional Disparities* (Toronto: James Lorimer and Company, 1978).

22. M. Olson, *Logique de l'action collective* (Paris : Presses Universitaires de France, 1978), and *Grandeur et décadence des nations* (Paris : Bonnel, 1983).

23. These strategic groups can sometimes produce goods and services as well. Olson (*Logique*) emphasizes that some groups, in addition to safeguarding the incomes of their members, produce goods and services to encourage collective action on the part of those who benefit automatically from improved incomes. Obviously, the strategic groups to which we refer can hold concurrent objectives beyond the bounds of their group interest, so that the Quebec trade union movement fights for legislation to improve the lot of all workers. Nevertheless, this analysis

focusses on the economic consequences of pursuing these two objectives.

It should also be emphasized that our definition of strategic groups differs from Olson's notion of groups with redistributive intentions, since the groups to which we refer pursue improved incomes as well as economic security. While groups' efforts to improve income cannot be denied, their interest in economic security is not always recognized. Even Olson, who has studied group behaviour extensively, neglects to emphasize this point.

24. This result can be deduced through the use of game theory. Neither case is a zero-sum game, since there is collaboration or negotiation between the actors in the first case, and each acts alone in the second. See A. Schotter and G. Fchwodiauer, "Economics and Game Theory: A Survey," in *Journal of Economic Literature*, June, 1980, Vol. XVIII, No. 2, pp. 479-527.

25. Those who would bypass the negative effects of strategic groups by seeking their destruction, in order to achieve perfect competition based on the theoretical efficiency of 'laissez-faire', cherish a utopian vision of reality. By now, the forces that gave rise to strategic groups are so well established that their abolition could only be achieved through recourse to a police state.

26. Although the argument in support of this thesis is based on the work of Thurow, we do differ with Thurow on this corollary, in that he presumes a game in which social gains are small but each group can expect to achieve important gains or losses. See L.C. Thurow, *The Zero-Sum Society* (New York: Penguin, 1981).

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DISCUSSANTS

David Wolfe — University of Toronto

We have much to learn from the experience of other countries that have made commitments to maintaining full employment throughout the post-war period, and most recently in the past 10 to 15 years. But as a political scientist, I would emphasize a broad perspective on employment, rather than a strictly economic one. In all societies, questions of economic policy are fundamentally questions about political choices.

Fundamentally, the economic policies we make in this country, or in any country, reflect political choices about the available alternatives. But those political choices are not made in some kind of idealistic world of economic theories and policy alternatives, theories about institutional structures and the policies they can formulate. They are made in the real world of politics, in which competing classes and political organizations, such as trade unions, strive to put forward alternatives and influence those that are chosen.

If we look closely at the experiences of countries that adopted full employment policies, we find a fairly high correlation between certain political characteristics and the kinds of policies those countries have chosen. Virtually all of them have large and very well organized trade unions, highly centralized union movements, and very close links between unions and social democratic labour parties. Often, trade unions have been able to form effective political alliances with elements of other social classes, as in Sweden for most of the period since the 1930s, so that institutional policies are a function of the political alliances and the balance of political forces that exist in those countries.

It is clear that this situation does not exist in Canada. In fact, we face a very different kind of political situation. So the fundamental dilemma that we face, given the political realities of this country, is how to begin organizing toward a situation in which we can begin to change some of the circumstances in which we currently find ourselves. This question is fraught with many political problems and difficulties but if we confine our discussion of full employment to the technical models put forth by various economists, focussing solely on which variable or set of assumptions to plug into our models, we will remain on the level of analysis done by the Department of Finance and the Bank of Canada and will get no further towards a real solution to unemployment. I do not claim to have a blueprint for political organization or action, but I have a fairly strong sense of the direction we need to go in order to effect these changes.

That direction is largely summed up in *The Other Macdonald Report*. Not the Macdonald Report as such, which I consider biased, intellectually suspect, and one of the greatest political travesties imposed on this country in the past

40 years. Rather than citing from that great writ, I refer to the work of organizations like the Social Planning Councils of Ottawa-Carleton and Metropolitan Toronto. In their introduction, the editors of *The Other Macdonald Report* suggested that there is a real and effective alternative to the policies followed in this country, an alternative that was presented time and time again to the Macdonald Commission. It is reflected in a consensus which is clearly shared by a broad number of social and political organizations in this country, spanning the voluntary sector, the trade union movement, and some religious organizations. It is a consensus around which those groups need to organize much more strongly and coherently than they have in the past.

If the organizations represented in *The Other Macdonald Report* begin to organize around these policy alternatives, this country will not have to live with the incredibly passive and negligent views of the professional economists, some of which are reproduced in Section III. It should be remembered that these authors are considered to be among the more progressive economists in this country. If this is the best they can do, and if we listen to them, none of us will have any impact on the problems we face.

Gilles Paquet — Dean, Faculty of Administration, University of Ottawa

The difficulty with a strict comparison of economic systems is the assumption that if we adopt a full employment policy, entrench participation by a broad cross-section of groups, find out how to motivate them and make them committed, then institutionalize the whole process and administer it in a decentralized way, we will have no problem. This reminds me of the fable about the very wise owl, to whom a fox came in the middle of winter, saying: "I have a problem. I am red, I run on snow that is white, and the hunters all shoot at me." The owl paused and said: "It's very easy — just change the colour of your fur from red to white, so that people won't see you or shoot you." The fox went away happy, but came back five minutes later, asking: "How do I do that?" "Sorry," the owl said, "I'm just a policy advisor — for technical details, you'll have to go elsewhere."

This is not the problem that Diane Bellemare and Lise Poulin Simon were asked to address, and if any of us really knew how to change the world, we would truly be well off. But my real worry is that, while the full employment study is long on diagnosis, while I like and share the diagnosis and think that it is very well developed in the paper, it does not help us build a different country. Canada has a small, open, and very dependent social economy; transforming it overnight is going to be very hard.

The study presents the right blueprint for change, but how do we tackle the reality that we face? We need a very wide and large market to survive. We need to be flexible, but that becomes very painful when it gets translated into details. If we talk about job creation, when the Americans decide to adopt

serious protectionist measures against our lumber industry, there are as many as 60,000 jobs at risk. When we talk about potential job destruction and compare that with job creation alternatives we get a better idea of what is happening in Canada. I am not defending the Mulroney government. But in this country, I would consider it reasonable for a pragmatic Prime Minister of any colour to initiate a discussion around market access, not to promote free trade as an end in itself, but recognizing that we should negotiate before the other side does something to hurt us.

The debate becomes theological when people make the most extraordinary assumptions about the content of a new social contract in order to disparage it. Disparage it in the name of what? In the name of doing nothing. But doing nothing is what is not tolerable. There is broad agreement that we need the world economy, and we need to be flexible. But there is no clear panacea.

In that sense, one of the central questions has been put in the full employment paper. It explains how interest groups' efforts to protect themselves have created a series of structural rigidities that cannot be simply washed away. It is quite clear that we want happiness and money, but it seems that we want security more than anything else. But if security is in fact our first goal, the thing we want at all costs, then we as a country are dead in the water internationally.

If security is our goal, and we grasp the idea that we are in fact no bigger than California, then instead of thinking of ourselves in terms of a world power as the Pearson types did, we have to talk about Canada as a small, open, dependent economy. But while we need to adjust quickly, we have all sorts of reasons for doing nothing, and we have interest groups and unions with motivations that I think are not entirely wrong.

I am not in favour of destroying 25,000 jobs, or 250,000 jobs. But I'm not pleased Premier Peterson predicts that 281,000 jobs will be lost as a result of free trade, and someone else says 110,000 and we get into a numbers game that discredits everyone. On the other hand, I think it is perverse to deny that some adjustment will have to be made.

My sense is that the Macdonald Commission is a very good beginning, but do not just read the final report if you want to understand the Commission. Volume 13 of the Commission's research studies, by Richard Harris, is a very nice starting place for a responsible discussion. From a theoretical point of view, Harris says we should throw out the whole theory of comparative advantage, recognizing that it may apply to natural resources but not to manufacturing. Harris makes some very bold statements in an attempt to construct our thinking about industrial strategy on a different basis.

The question of choosing what to save and what not to save was ignored by the Commission, but for me the Royal Commission report itself is not important. We all have our ideologies, we have our view of the world, and I do

not deny anyone's right to their beliefs. But in that mammoth study there are elements of answers. I would prefer not to defend today's institutional status quo as a virtue. I do not say that we should do nothing, that we should not sit down and negotiate with the U.S. for fear that we might lose. I am as nasty as anyone, and its seems to me that if you don't like the deal you're getting you just walk away and go home. It is wrong not to talk about a trade deal on the grounds that it might have to include safety nets or transition assistance for some of our people. If we really believe that flexibility is the foundation of the new international division of labour, then we must not start by being inflexible.

Fighting Unemployment: The Community's Role in Job Creation

Discussion of the community's role in employment creation, like any other subject in Canadian political life, focuses very rapidly on relations between levels of government.

David Ross, in presenting the Canadian experience with local economic initiatives, is careful not to overstate the employment benefits to be gained from these new ways of organizing economic activity. But he suggests that these new, in a sense hybrid, forms of enterprise merit attention from policy-makers at every level of government.

Penina Coopersmith presents a very concrete proposal from the Federation of Canadian Municipalities to use the much-needed renewal of urban infrastructure as an employment creation program. This would obviously entail major participation by the provinces and the federal government.

In his comments, John Calvert stresses the theme of power. The opportunity for local authorities to effect major change is not in question, but their capacity to implement such programs is more problematic. Municipal services are labour-intensive and meet human needs, yet they are being cut back at a time when unemployment is severe and needs are going unmet. Calvert sees this as part of the larger political agenda in Canada, where major corporations hold great sway at all levels of government.

The question of power is recognized by the other discussant as well. Richard Stewart zeroes in on the problem of the problem of the chronically unemployed, those who have been least able to benefit from existing employment initiatives. He holds out more hope for local economic programs than for larger-scale interventions, on the basis that, for the chronically disadvantaged, small *is* better.

IV

CONCRETE BENEFITS: JOB CREATION THROUGH PUBLIC INVESTMENT

Penina Coopersmith
Executive Director, Canadian Water & Wastewater Association

Introduction

This paper examines a relatively modest, but not insignificant contribution to easing unemployment: public sector investment in the upgrading and repair of municipal infrastructure. Specifically, it describes a program originally proposed by the Federation of Canadian Municipalities (FCM) in 1985 for a $12-billion investment spread over a five-year period that would create an average of 45,000 to 60,000 jobs per annum.[1]

The use of public funds to construct public works is far from being novel. It is a tried and tested means of easing unemployment, while improving the quality of life in towns and cities and increasing their capacity to support economic growth over the long term.

The idea of rehabilitating — or, in some instances, reconstructing — municipal public works has essentially the same attributes. The only difference is that genuine rehabilitation needs can be assessed more reliably than new needs (particularly on a national scale), and that the failure to undertake needed repairs results in measurable costs, while the failure to construct new works can be assessed only intuitively.

Despite its clear benefits, the proposed rehabilitation program (which cannot be financed exclusively by municipalities, due to their provincially and

federally imposed fiscal position) has gained support provincially but not federally. Instead, public sector capital investment is derided as a deficit-increasing luxury the nation cannot afford.

Given that the proposed program differs little from historical examples of such public investment — except that, in these times of economic stagnation as opposed to an acknowledged depression, prices have not fallen — it seems reasonable to look carefully at the program to see whether affordability is the real reason behind its rejection.[2]

This paper examines the scope of the current municipal infrastructure problem and the need for action, then turns to the benefits and costs of ameliorating the situation — or of failing to do so. Finally, it deals with some questions that arise from the failure thus far to establish such a program.

The Need

Infrastructure is the underlying framework of a system. Municipal infrastructure is the guts of our towns and cities. It includes such public works as roads, sidewalks, bridges, sewers, water supply and distribution networks, waste collection and disposal facilities, libraries, parks, schools and transit systems. Most of these, along with many other types of infrastructure, are built by municipalities, which use a considerable portion of their budgets to operate and maintain them.

The ability of a community to flourish depends on the condition of its infrastructure. The health and welfare not only of its citizens, but of its economy, requires sound, smoothly functioning infrastructure.

In recent years, circumstances have combined to create problems for municipal infrastructure. Primarily for political reasons, the pressure placed on local government budgets during the rapid inflation of the 1970s was not matched by municipal tax increases or (for a similar set of political reasons) by increases in provincial grants. The reluctance of municipal officials to borrow at high interest rates, the need for increased social spending during the recession and the virtually total withdrawal of federal spending for municipal infrastructure in the late 1970s all contributed to the lack of required capital.[3]

In addition, many municipal facilities — a large proportion of which were built in the post-war urbanization boom of the 1950s — are nearing the end of their lifespan. Some officials also point to red tape and delays caused by increased public involvement in decision-making as factors that have increased costs and led to a reluctance to invest in capital projects.

For all these reasons, in the mid to late 1970s, municipalities began to cut back on maintenance, thereby causing more rapid deterioration. Delays in repair and replacement increased operating costs, while compounding the eventual price tag for renewal.

In recognition of this situation, the FCM established a Task Force on Municipal Infrastructure in June, 1983 to assess the magnitude of the problem and develop strategies to deal with it.

Assisted by a technical committee of senior municipal officials (primarily City Engineers), the Task Force embarked on a survey of the state of municipal infrastructure. Based on the survey findings, in January, 1985, the Federation published a study entitled *Municipal Infrastructure in Canada: Physical Condition and Funding Adequacy*, as Volume 4, Number 1 of its "Municipal Dimensions" series.

FCM Infrastructure Findings

The study concluded that we have a significant problem in Canada. Although the situation is far better than in the United States — where estimates place the cost of bringing infrastructure to acceptable levels as high as $3 trillion — here, too, such essential facilities as roads, sidewalks, bridges, sewers and water mains are in the poorest condition and are deteriorating, rather than improving.

Nonetheless, it was noted that the need to reconstruct our municipal infrastructure provides an opportunity to strengthen Canada's economic recovery while, at the same time, employing large numbers of Canadians in work which, for the most part, is labour intensive. Accordingly, the study recommended that:

1) Steps be taken to halt the trend toward infrastructure decline;

2) The Federation direct its task force to identify specific policies and programs for corrective action to achieve this aim;

3) Programs be established to begin implementing these policies;

4) An intergovernmental partnership be established, to engage the combined and cooperative efforts of the three levels of government in solving the infrastructure problem;

5) Public awareness of the problem be increased, to obtain support for the necessary remedial measures;

6) Without jeopardizing the provision of new facilities to meet growth, a greater emphasis be placed on maintenance and reconstruction as opposed to new construction, in order to extend the life of existing facilities.

The study concluded that the cost of bringing the most seriously deteriorated infrastructure (roads, bridges, sewer and water systems) to acceptable levels would be high. In communities with populations over 100,000, the program would require about $680 per capita (in 1984 dollars). The costs in smaller municipalities cannot be estimated on the basis of current data, but

are acknowledged to be considerable. The study recommended a $12-billion, five-year program to bring municipal infrastructures up to standard.

The study also noted that the major responsibility for financing municipal infrastructure lies with local governments and users. But it concluded that the cost of the necessary repairs identified in the study — which represent an *additional* $12 billion beyond municipalities' basic projected spending on public works, or about a 6.75 per cent increase in total municipal budgets — is too substantial to be borne exclusively by municipalities. Accordingly, the study recommended that:

7) Jurisdictional barriers between local, provincial, and federal governments be minimized;

8) Financial assistance be sought from provincial and federal governments, especially for works having provincial or regional benefits;

9) Additional local government funding sources, including new methods of financing capital works, be found to help resolve the revenue shortfall problem.

Funding Not the Only Problem

The study concluded that, while funding is the primary cause of infrastructure decline, there are a number of other impediments to proper maintenance and rehabilitation. These include political inaction, excessive red tape, overly stringent conditions on federal and provincial government funds, prolonged public involvement, lack of staff and, for some facilities, the lack of appropriate techniques for problem analysis and proper maintenance. Accordingly, the study recommended that:

10) Methods be investigated to reduce waste and excess costs due to delays, red tape and other impediments to the reconstruction and maintenance of infrastructure;

11) Work begin on setting service standards in order to achieve some national consistency in assessing infrastructure needs and service levels. This should be done in concert with the U.S. and European countries, where such work is already in progress. This is a long-term effort — rebuilding infrastructure must not await its completion;

12) National associations be strengthened, to foster the exchange of information among Canadian municipal officials, and to publish manuals on information handling, acceptable level-of-service indicators, technical maintenance strategies and other infrastructure management practices;

13) Better information systems be developed, particularly for use in smaller municipalities, to permit better management of infrastructure systems and more effective use of funds.

In brief, then, there is a problem of substantial magnitude. There is a major shortage of funds and a need for information. There is also a recognition of the problem and a willingness on the part of municipalities to deal with it.

To achieve the aims set forth in the recommendations, the Federation adopted a two-pronged approach. On one hand, throughout 1984, 1985 and 1986, it met with appropriate federal ministers and, through affiliated provincial municipal associations, with provincial ministers, to establish a cooperative plan for tackling the infrastructure problem. This is a continuing effort.

At the same time, it proceeded to obtain more information on the problem. In particular, it focussed on the costs, benefits and affordability of a program to address the situation.

Costs, Benefits, Affordability

One of the most significant costs is clearly that of *not* undertaking the program — of postponing needed repairs indefinitely. Anything we don't fix now will cost more to repair or replace later. The old saw, "A stitch in time saves nine", certainly applies to infrastructure. American studies have shown that the cost of repairing roads and other facilities increases at an alarming rate after the structure reaches a certain age.

For example, one study estimated the cost of routine maintenance of good pavement to be about eight cents per square foot, whereas the cost of rehabilitating failed pavement is in the order of 80 cents per square foot. The World Bank compared strategies of resurfacing pavements every 15, 20, or 25 years, and found the annual cost per square foot to be 53 cents, $1.00, and $1.44 respectively.

To take another example, if a given piece of road will deteriorate to the point of total failure when it is left without maintenance for 16 years, the quality of the road will decline 40 per cent over the first twelve years, then suddenly drop an additional 40 per cent during the last four years. Each dollar that should have been spent during the first three-quarters of the road's life will cost between $4 and $5 in the last quarter.

Roads have been targetted for study because they present the worst examples of infrastructure deterioration in Canada, as in the U.S.. Roads are in an aggravated state of disrepair due to high-frequency use and age. Bridges, too, are beginning to show problems — often from the use of salt as much as age. Other facilities, like water supply and distribution systems, often average less than 40 years of age and have serious, but smaller problems.

It should be noted, however, that the costs examined above represent only the *direct* cost of delayed maintenance. The indirect costs are more difficult, if not impossible to assess. In one large Canadian city, for example, several major bridges have been declared unsafe for transport trucks and transit vehicles. This slows traffic, increases congestion and adds to the wear and tear on other facilities. It also may slow the economy of the city by deterring

trade requiring good transportation routes, but the actual cost involved cannot be quantified.

In another city, a decaying water system is developing up to 20 leaks a day, interrupting water supply to homes and industries within a 100-block radius while repairs are made. The cost of the repairs can be calculated easily, but the costs in time and productivity loss throughout the affected area are incalculable.

Infrastructure Program Impacts

The January, 1985 study on physical condition and funding adequacy had highlighted the value of infrastructure improvement as a means of creating jobs. The first question posed by journalists, Members of Parliament, and FCM members was, "How many jobs?" The second question was, "What will be the effect on the deficit of this capital investment?"

To answer both questions, the FCM retained Informetrica Ltd., a consulting firm specializing in economic analysis and forecasting. Their report, *The Macroeconomic Impact of Accelerated Spending on Municipal Infrastructure*, was issued in mid-1985 as Volume 4, Number 2 of FCM's "Municipal Dimensions" series.

Informetrica's analysis included an examination of the direct, indirect and induced effects on the national economy of spending $12 billion over a five-year period beginning in 1986. In addition to employment, the study examined the effects on the deficit, inflation, interest rates, wages, industrial output and on household, business and government expenditures.

For the purposes of the analysis, it was assumed that the $12-billion spending program would be spread evenly over a five-year period, and that each level of government would contribute equally to the program.[4] Allowing for an anticipated average annual inflation rate of 4.2 per cent, the nominal expenditure would total $14 billion, or roughly 0.5 per cent of the GNP per year.

It was further assumed that this reconstruction program would represent an *additional* program for municipalities, equivalent to 45 per cent of what municipalities would allocate to capital expenditures in any case. Varying municipal circumstances result in differing views on the extent of infrastructure deterioration, and on the priority that should be accorded to rehabilitation. In keeping with the earlier report's findings on the condition of different facilities, the study assumed that approximately half the expenditures would be allocated to the repair of roads and bridges, with the other half split between sewer and water systems.

In calculating the impact of this investment on expenditures, output, employment, inflation and incomes, two cases were considered. In the *High Impact Case*, it was assumed that all three levels of government would borrow the full amount of the funds required. It was also assumed that the funds

would be obtained from abroad (or that other capital requirements would be provided from foreign sources to compensate), with no significant effect on Canadian interest rates.

In the *Low Impact Case*, it was assumed that local governments would impose taxes and increase user fees to cover part of their share of the increased spending. It also was assumed that borrowing by municipalities and the other orders of government would have an adverse effect on capital markets, in the form of increased interest rates. Both cases were measured using Informetrica's December 1984 "Base Case".

The report concluded that there would be a positive impact on economic output, employment and incomes in each year of the spending program. In the *Low Impact Case*, real economic activity would increase by about 0.5 per cent in each year of the program. In the *High Impact Case*, real economic activity would increase by about 0.7 per cent.

Since direct expenditures for municipal infrastructure are principally for equipment and construction labour, the main industrial benefits — more than 55 per cent of the total change in economic output — would accrue to the manufacturing and construction sectors. However, all other sectors could be expected to show some positive effects as a result of increased personal consumption, business investment in enlarged facilities, and the residential purchases and improvements that would be stimulated by higher household incomes.

The effect on government deficits would depend on the financing options chosen. Most experts agree that the total impact on the economy would be positive, and some postulate that the impact on the deficit would also be good. In the event that each level of government funds its one-third share of the program through debt, and there is no adverse effect on interest rates, Informetrica concluded that the impact on federal and provincial balances would be positive, or only slightly negative. By contrast, there would be a negative impact on municipal balances in each year of the program.

It is estimated that the program would create between 220,000 and 285,000 person-years of additional employment. Here, too, the variation is based on the funding arrangements and the impact of the spending on interest rates. In the *High Impact Case*, new employment would grow from 30,000 jobs in the first year of the program to more than 75,000 in the fifth. In the low case, employment would increase by slightly under 30,000 in the first year and rise to about 55,000 in the fifth.

In either case, employment in manufacturing and construction — the sector that ranks second only to forestry in unemployment rates (20.5 per cent in 1982, 23.9 per cent in 1983, 22.7 per cent in 1984)[5] — accounts for 55 to 75 per cent of the increase.

At the very least, the cost and the increase in economic activity balance out, allowing the program to pay for itself as work proceeds. The report notes

that the expanded economy, buoyed by more jobs and spending, would increase government revenues (through taxes on income and materials) and reduce some expenditures (such as UIC), permitting governments to recover some of their initial outlay immediately. The effects on jobs, incomes and output are on the high end of the scale compared to other forms of government expenditure, because about 90 per cent of the required materials are available in Canada.

Even in the worst possible case, in which the program leads to increased costs through higher interest rates or initial increases in deficits, the three levels of government would share a combined cost of about $6 billion, inflation included. As Informetrica pointed out, "as the spending program would cost more than $14 billion, inflation included, this implies that about $8 billion would be recovered from the initial expenditures through improved economic activity."

The data also show that increased government expenditures on municipal infrastructure can create 300 per cent more jobs than a comparable cut in corporate or personal income taxes and that the debt impact is far less.

In fact, in comparing capital expenditures for municipal infrastructure with other possible government expenditures, only policies that directly reduce Canadian prices would have a clear, comparative advantage in terms of employment and government deficits.

Questions about the Program

The municipal infrastructure rehabilitation program proposed by the FCM would improve the quality of life in communities, provide jobs in a sector suffering from particularly high unemployment rates, and contribute to the capacity of towns and cities to sustain long-term economic growth. At the very worst, it would result in a feasible government spending program which would surpass all others in its positive impact on jobs and the deficit.

Yet two questions remain. The first is whether, despite these attributes, public sector investment is appropriate at a time when some economists would have such expenditures cut back in order to reduce the deficit. The second is whether the federal government should be involved in funding municipal infrastructure.

With respect to the first, cutbacks have already been made in precisely this area. The FCM study on funding adequacy demonstrates that municipal public works budgets have declined as a proportion of total local government spending, from 31.9 per cent in 1968 to 26 per cent in 1983.

Even more dramatic has been the decline in real capital expenditures by all levels of government. Spending has increased by about 2.5 per cent since 1975, although the real economy expanded by about 26 per cent during the same period. Public sector investment between 1960 and 1982 dropped as a percentage of total capital expenditures from 15 per cent to 9.5 per cent.[6]

As for the second question, there are at least three major reasons that the federal government should invest in municipal infrastructure. First, Canada's communities themselves are, in effect, part of the national infrastructure. If they cannot function efficiently, the national economy suffers. As economist Arthur Donner has pointed out, "A deteriorating public infrastructure unnecessarily increases unemployment, damages Canadian industry's ability to compete in foreign and domestic markets, retards domestic productivity and imposes inconveniences and higher costs on the general society."

Moreover, in terms of national and international trade, there must be some attention to the capacity of towns and cities to handle such trade. It can be argued, therefore, that equalization is as much an issue with respect to essential public works as it is with health care, higher education or industrial growth. Considered in this light, municipal infrastructure seems an ideal candidate for support under Economic and Regional Development Agreements.

Second, the Informetrica study shows that, in the *High Impact Case*, the federal government gains more from the program than provincial or local governments. Its balances would increase in the first, third, fourth and fifth years of the program by $160 million, $380 million, $80 million, and $840 million respectively. Were the federal government to withold its contribution, the negative impact incurred by municipalities under the best of circumstances would be increased. It is also possible that as a participant in the program, the Government of Canada might think twice about imposing new taxes on the materials required for infrastructure improvement — the 1985 and 1986 budgets each imposed taxes that raise the base cost of the overall program from $12 billion to well over $14 billion.

Third, municipalities will require research to determine which facilities are most in need of repair, and to develop new maintenance techniques and technologies. Such research should receive federal support, as it does in every other western nation.

Returning to the appropriateness of such an investment, there does not seem to be any reason to consider the use of public funds to construct public works any differently today than in the past. On the contrary, common sense suggests that continued deterioration of municipal infrastructure will hurt not only individuals, but the prospects of economic renewal.

Clearly, "reason" cannot explain the failure to undertake the recommended program. More to the point is the patently absurd notion that a combination of tight money policies, shifting wealth to the well-off, deregulating the private sector and "downsizing" government will result in increased capital investment, increased productivity and increased jobs.[7]

Yet even for those who hold to the mythical belief in the powers of the private sector to remedy all economic ills, it should be evident that the work needed to bring Canada's municipal infrastructure up to acceptable levels

will not be undertaken by the private sector. Nor will it take the form of "community" projects or voluntary efforts.

Though the proposed program can only make a small contribution to the overall problem of unemployment, the government response to date demonstrates the hollowness of the electoral promise of "jobs, jobs, jobs".

NOTES

1. The data for this paper are taken largely from *Municipal Infrastructure in Canada: Physical Condition and Funding Adequacy*, a study commissioned by the FCM and published as Volume 4, Number 1 of the Federation's "Municipal Dimensions" series; from *The Macroeconomic Impact of Accelerated Spending on Municipal Infrastructure*, a report prepared for the FCM by Informetrica Ltd. and published as Volume 4, Number 3 of the same series; and from *Work, Work, Work*, a brief report on the upgrading of municipal services published by the FCM's Municipal Economic Development Program in the summer of 1985.

   Penina Coopersmith assisted in the preparation of terms of reference for all three reports, served as editor of the first volume, and authored the executive summary for the second.

2. A second difference lies not in the program, but in the size of the deficit. This paper does not address the question of whether it is dangerously large. Rather, it examines the likely impact of the program on the deficit, and some of the long-term costs — which might actually increase the deficit — of failing to implement it.

3. The history of federal support for municipal infrastructure is surprisingly difficult to unearth. A good short summary of funding for municipal water and sewage works may be found in James W. MacLaren, *Municipal Waterworks and Wastewater Systems* (Research Paper #3 of the Inquiry on Federal Water Policy, pp. 27-28). Information on other municipal services is contained in *Urban Infrastructure in Canada*, the unpublished, technical report that formed the basis for *Municipal Infrastructure in Canada: Physical Condition and Funding Adequacy*.

4. This was the model proposed to the federal and provincial governments. The typical 50-25-25 split for earlier programs placed a greater burden on the federal government.

5. Statistics Canada, *Labour Force Annual Averages*, Cat. 71-529, (Ottawa: Government of Canada, February, 1984) and *The Labour Force*, Cat. 71-001 (Ottawa: Government of Canada, January 1985).

6. From Statistics Canada and Department of Industry, Trade and Commerce, *Private and Public Investment in Canada*, occasional, Cat. 61-504

and annual, Cat. 61-206.3. In John Calvert, *Government, Limited* (Ottawa: Canadian Centre for Policy Alternatives, 1984).

7. This is the view in the U.S., where the Reagan administration is being widely hailed for having spurred economic growth. But a quick look at just a few comparisons between the Carter administration (1976-80) and President Reagan's first term illustrates that things are less rosy than is generally claimed*:

   Real growth in GNP dropped from 13.6% to 11.1%,

   Industrial growth dropped from 12.6% to 11.1%,

   Fixed business investment dropped from 32% to 23.4%,

   Average, non-farm private weekly earnings dropped from $183.62 to 170.74,

   Federal interest as an average percentage of GNP rose from 1.7% to 2.7%,

   The percentage of Americans living in poverty rose from 11.9% to 15.2%,

   Civilian jobs created dropped from 10.6 million to 5.7 million,

   The average unemployment rate (a figure increasingly contested as erring on the side of underestimating the problem) rose from 6.5% to 8.6%.

   * These figures were reported in *In These Times*, May 15-21,1985.

V

LOCAL ECONOMIC INITIATIVE: AN OVERVIEW

David P. Ross
Policy Associate, Canadian Council on Social Development

For some time, the Canadian Council on Social Development has been concerned that full employment, the fundamental assumption on which the functioning of the welfare state is founded, can no longer be taken for granted.

In the post-war era of sustained economic growth, a free enterprise system assisted by selective government intervention provided unprecedented increases in material prosperity. Most of this prosperity was associated with the expansion of stable, well-paying employment opportunities. Individuals and households that could not get aboard the economic juggernaut improved their standard of living through welfare-state social security provisions such as Old Age Assistance, Canada/Quebec Pension Plans, social assistance, unemployment insurance, family allowances, child tax credits, public housing, and medicare.

The welfare state worked reasonably well as long as the overwhelming majority of Canadians drew social and income security through their expanding paycheques. But as unemployment increased during the 1970s and remained high in the 1980s, and as economic growth slowed, governments found it increasingly difficult to accept (or to pass on to taxpayers) the growing costs of publicly assisted social programs.

Now we witness sustained attempts to cut back on hard-won and previously accepted social security practices and benefit levels. The elderly are

asked to forego full indexation of the universal Old Age Security (OAS) pension — the cornerstone of Canada's pension system. Full indexation of family allowances is no longer deemed possible. We question whether maternity benefits should be part of our social insurance system. Unemployment insurance recipients are increasingly suspected of being idle loafers, and the whole UI scheme is in danger of becoming a welfare program based on need, rather than an insurance program based on entitlement and right. Social assistance, administered by the provinces, is undergoing cutbacks, to the extent that single individuals in some provinces receive about $100 per month to take care of all their needs. Doctors are opting out of the formerly universal health care system, and hospitals are resorting more and more to fund-raising charity drives to cover deficits. The federal government is withdrawing from the provision of social housing, and provincial governments are squeezing post-secondary educational institutions and closing public schools.

This is the crisis of the welfare state. At the centre of this crisis is the quality and quantity of employment opportunities. Since we can no longer rely on the traditional mixed economy to provide full employment and sustain welfare state activity at expected levels, we must now seek new ways to create jobs and provide income security. One promising avenue is local economic initiative (LEI), a process that amalgamates economic and social concerns.

The process is based on unconventional business activity, as defined by five criteria used commonly to describe conventional, commercial business activity:

1) Motive,
2) Financing,
3) Structure,
4) Organization,
5) Nature of output.

Motive

The motives for establishing a LEI enterprise vary, but always differ from the profit motive of conventional businesses. Strong social or environmental concerns are often at the root of a LEI enterprise. Examples would include persistently high unemployment rates; regional depression, frequently caused when a major company closes down or a natural resource is depleted; chronic employment difficulties faced by the disabled, mothers on welfare or natives; lack of local training opportunities; inadequate provision of basic needs; or a desire to do something creative in and for the community.

An Ottawa community development association established a restaurant in an attempt to fill a crucial neighbourhood need for training and work

experience for disadvantaged youth. The motive is social, but the means is a commercial establishment that provides 22 weeks of on-the-job training in food preparation, food service and bartending skills. It relies on a government Job Corps grant, supplemented by operating revenue.

It is hard to imagine a conventional business established to train disadvantaged youth in a low-income neighbourhood. What is novel about this restaurant is the attempt by a community organization to merge private economic objectives and public social concerns, through a community-owned business that is not guided solely by profit. The public grant permits management to make some decisions based on social factors, while revenue from the restaurant's patrons provides a degree of long-term independence as well as a criterion to judge whether the business side of the operation is succeeding.

The degree to which a local economic initiative is able, or willing, to meet difficult social needs at the expense of conventional business practices and profitability will usually depend on the proportion of public money as a share of the total revenue. In some cases, social needs can be met entirely through operating revenues, with no need for on-going public support. But generally, the more difficult the social need, the greater the requirement for public money.

A strong case can be made for continued public support of particular local economic initiatives, when these initiatives are dealing with social and environmental concerns. The costs of social and environmental problems arising from the business practices of traditional commercial enterprises are ultimately assumed by the state, the voluntary sector or the public at large.

Two societal costs result from problems like unemployment, drug abuse, alienation, marital distress, crime, poverty, ill health, industrial accidents and pollution. The first is a reduction in quality of life for the general public. Unresolved problems inevitably impose costs on the public in the form of aberrant and threatening behaviour, drunk driving, crime, and child abuse, to give but a few examples.

The second cost is the money required to resolve the problem. Canada now spends about $40 billion per year on social programs. Not all this money is aimed at alleviating downstream social problems. Still, it is legitimate to consider transferring at least several billion dollars per year in an attempt to tackle social problems on a preventive basis, through the local economic initiative process. If local economic initiative can diminish social problems and their associated costs, it makes sense to supplement the commercial revenues earned by local enterprises with a sizeable portion of social funding. Clearly, assistance to local economic initiative does not require a net increase in government spending. On the contrary, it is a more effective upstream allocation of limited public funds.

Financing

Conventional businesses obtain their venture capital or start-up funds from commercial banks, owner and family investments, or public shares. But LEI enterprises more frequently rely on government through job creation, training, regional development and social service project funds. Social entrepreneurs often develop ingenious combinations of public and private financing to launch their businesses.

There is evidence that some credit unions are increasingly willing to support LEI, although banks remain steadfastly indifferent to this type of economic initiative. Funds can also be raised by individual subscription and local group donations. As well, municipalities are becoming increasingly involved in local initiatives that were originally dominated by the federal and, later, provincial governments.

In unconventional small businesses, worker cooperatives and collectives, a substantial amount of seed money comes from the participants themselves. Local community and church groups, as well as conventional businesses, have also supplied non-financial resources — space, material and business expertise. A local economic initiative needs to be exceedingly creative in putting together complex financing packages.

In Vancouver, a popular restaurant raised its start-up capital through workers' contributions, a loan from an interest-free credit union (which is in itself an unconventional financial institution specializing in the funding of workers' co-ops), and the sale of memberships to patrons who receive a discount when they dine at the restaurant. The next step for a successful unconventional business would be to purchase a large share of its produce and supplies from other enterprises created through local initiative, thereby creating a market for other unconventional businesses.

Structure

Most conventional businesses have fairly predictable and well-defined single-proprietorship, partnership, or limited-liability-corporation structures. However, there is no typical structure that results from local economic initiative, and new forms are constantly being developed. Some common structures include: worker co-ops, collectives, community development corporations, community enterprise centres, unconventional small businesses, business components of voluntary organizations, intentional communities, barter groups, and organized skills-exchanges. Credit unions are sometimes associated with the funding element of the LEI process.

A community development corporation in Nanaimo has set up a separate investment arm which exists solely to invest capital in promising local enterprises. This investment arm can choose the mix of social, environmental and economic concerns it wishes to support, as long as the overall investment portfolio sustains itself. Uneconomic but socially profitable enterprises can

thus be subsidized from the profits of purely economic enterprises. In this unconventional business structure, the semi-autonomous investment arm assures the long-term viability of the community corporation, while the parent corporation assures that its investments and proceeds are partially directed to meeting the community's social and environmental needs.

Organization

The organization of local economic initiatives is likely to differ from traditional business in terms of work practices and scheduling, management and decision-making, and distribution of rewards.

One of the motivations behind the creation of LEIs is the recognition that people require different workstyles and schedules. However, unless participants have a direct voice in the organization of work, significant flexibility and workstyle diversity are unlikely to be achieved. This is not to say that all hierarchical authority and work discipline can be abandoned in favour of purely consensual approaches and workplace anarchy. Discipline and authority come after participants have democratically arrived at workstyle decisions. Further adjustments are made as needs change.

An important organizational element that generally sets LEIs apart from conventional businesses is that the distribution of rewards, principally wages, is more equal. The reward structure is based on decisions taken by the participants. It is not decreed by so-called market forces, as in conventional businesses, although prevailing wage rates do play a role, along with wage guidelines set by government funding programs.

A multi-cultural catering service was established by immigrant women in Ottawa as part of a women's multi-cultural centre, which itself is partially funded by government grants. The commercial service is an outgrowth of the initial social purpose of the centre. Several women, from widely varied cultures, decided that they could join together to provide a unique and diverse catering menu. The women prepare the meals, sometimes at home, according to a flexible schedule that fits around their family and community responsibilities.

Nature of Output

Conventional businesses seek the most profitable market opportunities. An LEI business may incorporate profitable ventures, but will usually produce basic goods and services which are in short supply in the local community, but are ignored by the private and public sectors. LEI enterprises seek opportunities that yield high social profits, not necessarily high commercial profits. Twenty per cent of Canadian households receive only four per cent of Canada's total income, and most of these two million households cannot afford to pay commercial prices for basic needs. LEI businesses are frequently established to fill this neglected niche in the marketplace.

In Ottawa, and at least one other Ontario location, LEIs have chosen to produce comfort clothing for people with disabilities. Since many disabled people in Canada are geographically dispersed and have low incomes, the commercial sector has never paid attention to their special clothing needs. This is not a natural product line for conventional businesses, but it is for LEIs.

In Sydney, Nova Scotia, a community corporation funded a dental clinic after free market forces failed to attract adequate care. The local community-owned corporation could fill the gap because it was not seeking the maximum returns that dentists could only find in the Halifax area.

Conclusion

It should be stressed that a LEI enterprise need not meet all these criteria to be classified as an unconventional business. An enterprise that meets any three of the criteria would probably be considered an LEI.

In slightly more abstract terms, if an enterprise is small, uses cheap and understandable technology, is labour-intensive, and uses social accounting as its operating rationale, then it qualifies as the type of economic initiative that should be encouraged in order to address today's economic, environmental and social problems. It is through community-oriented economic initiatives, and the people they attract, that we may be able to permanently resolve the crisis of the welfare state.

DISCUSSANTS

John Calvert — Canadian Union of Public Employees

It is essential to look at what is happening at the local level in the context of the broader economic process. Extremely high unemployment cannot be fully or even fairly addressed in the local context without assessing the impact of federal government policies which, in my view, are deliberately designed to maintain this level of unemployment. So even as we look at this one area where we need to find some solutions, we might ask how much is possible without major changes at the national level.

One of the key problems is that, to a large extent, the community does not really control its own economic development, but is integrated economically and politically with wider regional, provincial, national and to some extent international economic trends and factors. These developments obviously have a very profound impact on everything that goes on within local communities. So, in some sense, I think it is fair to say that the community is very much at the mercy of wider economic forces beyond its control. What we are really discussing then, is the extent to which we can use the resources that are controlled by the community to develop some sort of economic policy that would create jobs. Since the community has little if any control over market forces, it is not in a position to plan its economic development in a sensible way.

Another implicit concern is the extent to which community initiatives develop or encourage a sense of self-reliance, or a community multiplier effect. Whatever we are thinking about in terms of economic development should be seen within the context of the national and provincial economies, and must reflect some understanding of these relations. But it must also aim to increase the community's ability to make decisions that put more resources back into the community.

This discussion is not just about economic measures, but about power over resources in the community. This is perhaps a fundamental issue that should be addressed more explicitly.

Another underlying assumption is that the private market has failed to create jobs in the community or address the employment needs of the people in the community. The development of enterprises or economic associations with non-commercial or non-business components is one way of ensuring that social needs are taken into account. In particular, expansion in areas such as worker cooperatives is long overdue. We really need to look at this area as a way of promoting community economic development.

But to do this, there are certain things that need to be clarified. One point is the overall framework in which these organizations operate. A key problem for many local economic development organizations is a very hostile

economic environment. In legislation, in the operation of the banking system, and so on, they are very much at the mercy of a whole range of factors well beyond their control. So while a strong case can be made for cooperatives, the regulatory environment, financial incentives and other forms of government assistance must at least equal what is provided for the private sector. Also, having said that, I do not think that these kinds of initiatives are the answer to unemployment at the local level. Rather, they arise because of a feeling that nothing can be done at the national level.

One important issue that has been addressed at the municipal government level is affirmative action, which I think is a vital part of any coherent job creation strategy. So often, we look only at the numbers of jobs, and do not think enough about who the recipients are; we do not think about effective ways of bringing people at the margins of society into the labour force. But governments' difficulties in trying to entice the private sector to include affirmative action in job creation programs are well known.

Another point that is quite relevant is the difficulty we face in making many of our public institutions responsive to community concerns about job loss. All kinds of roadblocks seem to arise when you have various levels of government trying to put together some sort of coherent program. On top of that, of course, in the last five or six years, fiscal restraint policies have hamstrung the ability, particularly of municipal governments, to take real initiatives. The need to fund infrastructure development is clear, and needs to be more widely understood.

Investment in public infrastructure is one way of channeling money into local communities to create new jobs, jobs which are good jobs in general and that will satisfy some very important community needs. But I would go much further. The whole role of the public sector in a community development strategy, a community job strategy, has become a very unfashionable subject in the last few years. Instead of using government directly to promote economic development at the local level, job creation has become a matter of subsidies to the private sector. We have cutbacks, year by year, in federal transfers to the provincial governments, and in provincial transfers to the municipalities, with the consequence that we have created a great deal of unemployment at the local level.

Not only is it time to rethink this cutback strategy, it is important to aggressively promote the position that direct government provision of services is one of the best ways to provide decent jobs for people. This understanding must be at the core of a really effective job strategy. Spending on hospitals, schools, public housing, social services, municipal services, and so on, should be increased because these institutions meet human needs, and the spending works — it creates jobs. It may be a simple way of putting it, but when you put money into the program you get jobs out at the other end. It is not syphoned away by some multinational company. It does not vanish in sleight-of-hand accounting. You actually create jobs.

Public sector employment projects, whether through municipal government, school boards, or other public institutions are very cost-effective in creating jobs — much more so, in general, than equivalent private sector subsidies, tax cuts, or other giveaways. This is even true of capital investment at the municipal level. Combining this point with the argument that communities' real social needs are not being met, can show convincingly that public sector employment does work and does satisfy those needs.

Finally, it is very easy to focus strictly on the number of jobs. But our economy has more and more part-time jobs, more and more contract jobs, more and more temporary jobs, and a whole generation of young people out there who have never experienced full-time work. One of the key virtues of putting money into public programs is that you are creating jobs with some degree of permanence for the people involved — jobs that do provide, if not a high income, certainly a decent income compared with some of the minimum wage or less-than-minimum wage jobs that are being offered in the "McDonald's" sector of the economy. We need jobs where people can think about and plan for their future in a sensible way. Through the public sector you can deal effectively with questions like affirmative action, and with the need to address certain target groups. This is a very important part of any full employment program.

There are certainly many problems with public sector institutions, at the local and other levels. There is no question that, in order to make new intitiatives work, we have to talk about a major reorganization of government at the local level. But we should not throw the baby out with the bath water by saying that the solution to the way government is administered right now is no government. The solution is to change the way government operates.

More discussion is also needed on the limits to community organization, recognizing that power is central to what is possible. Take what is happening with the unemployed, for example. Is the fact that they are not organized significant to the failure of local institutions to respond to their needs? Until they are organized, will this be a major contraint in developing political pressure to make job creation programs a political alternative? The whole question of community organization and power at the local level is fundamental, and must be dealt with.

Richard Stewart — Executive Director, Program Delivery,
Social Services Department, Regional Municipality of Ottawa-Carleton

In Ottawa-Carleton today, there are 9,500 recipients of General Welfare Assistance, two-thirds of whom are theoretically employable. Of the 6,300 people in that employable group, 91 per cent have less than high school education, 83 per cent are classified as non-skilled by virtue of their previous employment, 34 per cent are under the age of 24, 54 per cent are under the age of 30, and 40 per cent have not worked in the last 12 months. I am not

describing a group of people who are in transition from one job to another, the *cyclically* unemployed as we refer to them. What I am describing is the chronically unemployed, individuals who are chronically disadvantaged with respect to employment.

Local economic initiatives show the potential for providing self-determination at the local level by setting out the economic and social objectives of the various enterprises. The Social Services Department of Ottawa-Carleton believes firmly that local determination must be brought to the neighbourhood level. As such, we support the development of local economic initiatives through community service centres.

But while there is usually some mix of private and public funding and self-generating revenues for these enterprises, the extent of public funding is a concern to me. I have to ask, and I think others should as well, to what extent these initiatives can maintain their objectivity, retain their power for self-determination, and also receive public funding. The aims and objectives of public funding are not always directly contrary to those of community-based groups, but the potential is there. Moreover, it could be argued that there is an even greater potential for conflicting objectives when these public funds emanate from the provincial and federal treasuries, when they have "macro" social and economic objectives.

A case has been made for the transfer of social assistance dollars to specified local economic initiatives. I understand that the federal government is actively discussing this issue with the provinces. They are talking about the diversion of federally subsidized social assistance dollars into employment programs for public assistance recipients. This could, in some contexts, be a very positive initiative, but it could also be a recipe for disaster, leading to very regressive social policy and programming. Massive public works programs or workfare projects in California (particularly San Diego), and more recently in New York, require chronically unemployed welfare recipients to work involuntarily for the municipality or the state, in return for their public assistance. The evidence to date from these projects indicates that there is little or no provision of training or on-the-job skill development. The real benefit of the program is to the public treasury, for the goods and services provided by these people.

The positive side of the diversion, and it would likely be a diversion of public assistance dollars to employment creation, is that it would provide a basic budget to at least cover the wages for community economic development projects. In my view, the social objectives of providing needed community services, meeting employees' training and job development needs, and having the initiatives based on sound business practices must all be in place before any municipal, provincial or federal government should consider these diversion schemes. But even though community economic development deals with a small piece of the action, it may be the only piece of the action where local control can be achieved. And community economic development

or local economic initiatives are very promising solutions to some of the problems created by the crisis in the welfare state.

The importance of shifting real control and influence to the local level, be it a municipality, a neighbourhood or a community, is the key point. Without local input, many projects will fall far short of providing real employment opportunities for the less skilled and non-working poor. The most important consideration is that affirmative action directed at the chronically unemployed be backed up in future by strong policy controls.

Initiatives that combine the social objectives of both socially assisted housing and job creation, enable welfare recipients to keep a greater percentage of earned income before deductions, or embody a jobs-to-people strategy which creates neighbourhood employment opportunities, could all flow from an emphasis on local economic initiative. It is in the neighbourhoods and communities where chronically unemployed people live that a real commitment to social change must be accepted, and a job strategy has to begin. The proper municipal role is to support local economic initiatives whose social objectives include the provision of training for job opportunities, especially full-time employment. But because these initiatives do not provide a quick fix, they are not embraced by very many politicians at any level.

I am not about to challenge the potential for job creation through infrastructure renewal, nor do I challenge the need to fix the potholes in my street and all the other infrastructure that is going to rack and ruin. The need is obvious. I have serious reservations, however, about the potential for available jobs to improve the employment prospects of the chronically unemployed, unless there are clear policy guidelines and affirmative action programs. The hard core unemployed do not generally benefit from public works initiatives. Unless we keep watch, even if a major infrastructure program is initiated across Canada they will be neglected once again.

Inasmuch as they are in a position to deliver social services, influence development and growth, purchase large volumes of goods and services, and respond to rapidly changing economic and social realities, municipalities are in the best position of any level of government to foster the growth of local economic initiatives. This explains their importance in any full employment strategy.

The Big Picture: Can Macro-Economic Policy Reduce Unemployment?

Mike McCracken is one of Canada's foremost economic forecasters. His firm, Informetrica Ltd., is a widely respected advisor to government and business. In this article, he sets out the case for easing monetary policy, arguing that a made-in-Canada interest rate policy is an important element of employment policy and showing that it is a feasible goal. While simulations of the impact of such a policy do show that some initial inflation would result, the inflationary costs are small and would disappear quickly. Though McCracken's estimates of employment gain are modest, the important point is that North American monetary integration need not constrain Canada to follow a policy that leads it away from full employment.

Discussants of this article point out that McCracken's prescription is hardly reassuring to those proponents of full employment policy who would use monetary policy to achieve greater employment growth. Patrick Grady suggests the weight of opinion within the economics profession is against monetary stimulation. Sidney Ingerman finds that current economic wisdom is woefully inadequate with respect to the very real social problems facing Canada, and suggests that economists are much too smug in the face of human suffering. Ingerman says the sort of activist policy favoured by McCracken is eminently preferable to simply explaining why the status quo is the only satisfactory policy stance.

David Dodge, a senior official with the Department of Finance, notes that the policy climate in Canada has changed dramatically. Where once it was widely accepted that fiscal and monetary policy could produce full employment, and that the only question was how best to do it, we are now questioning whether such policy instruments can be effective at all. For Dodge, the important issues are the mix of fiscal and monetary policy and their inter-relationship. Without an appropriate fiscal policy, the use of monetary policy to reduce unemployment is compromised.

VI

IMPACT OF A MORE INDEPENDENT MONETARY POLICY ON UNEMPLOYMENT

M.C. McCracken
President, Informetrica Limited

Almost no one today is satisfied with the level of unemployment. The fact that at least one million people are not working is something that most of us find reprehensible. By not operating at the "potential" of the economy, I would estimate that we are leaving about $50 billion per year on the table. That is, if we were operating at an unemployment rate of five per cent or less, we would be producing about 10 per cent more real output (GNP) every year. In addition, the ledger should include a substantial allowance for the social costs of extended high unemployment. This includes the despair of those who have been unemployed for an extended period of time, who have lost hope and whose skills are atrophying.

At the same time, we all want to avoid as well the recent experience of 1980-1982. It is not desirable to go through another period of depression, coupled with extremely high interest rates.

A number of respected groups have recommended a move to easier monetary policy. In its 22nd Annual Review, *Strengthening Growth*, the Economic Council of Canada recommended a package combining monetary ease with further fiscal restraint. The Macdonald Commission also recommended a move to easier monetary policy sufficient to offset any shift to a less expansionary fiscal stance. In 1982, and then in 1984, groups of economists recommended lower interest rates as a necessary backdrop to a

lasting recovery. In 1984, we examined a policy package that included an easing of monetary policy as well as some fiscal stimulus, aimed at bringing the Canadian economy back to full employment within five years.

In recent years, interest rates have come down. Average rates in 1985 were lower than in 1984, and the 1984 average was lower than 1981 and 1982. But there is still dissatisfaction. While nominal interest rates have declined, inflation has dropped even more rapidly, so that today's real interest rates equal or exceed the real levels of several years ago. At this point, interest rates can only be reduced by holding nominal interest rates where they are and purposefully inflating the economy, or by reducing nominal rates and by an amount that exceeds the decline in inflation.

The problem is further complicated by the fact that real interest rates in the United States have remained quite high. Growing awareness of the inappropriateness of U.S. interest rate policy for Canada has led to calls for a more independent monetary policy. Today, this means that nominal interest rates in Canada would have to drop below U.S. rates if we want to equal or better their inflation performance.

In fact, the conventional wisdom is that Canada will only achieve lower nominal interest rates than the U.S. if our inflation performance was better than theirs. Implicit in this view is the assumption that real interest rates would be the same in Canada and the U.S., and for that matter elsewhere in the world, in the longer term. Another school of thought provides for deviations in real interest rates, but only following the appreciation of the Canadian dollar. For example, an expected two per cent annual appreciation would allow real interest rates in Canada to fall two percentage points below those in the U.S. The only other routes to independence are suggestions for exchange controls, tax wedges or subsidies to provide a gap between U.S. and Canadian rates. But controls are not likely to work, interest equalization taxes can be easily evaded, and interest rate subsidies are an expensive way to create jobs.

It would appear that we can pursue an independent monetary policy by allowing the exchange rate to be fully flexible. In the short term, a drop in Canadian interest rates relative to the U.S. would lead to a lower dollar. In the longer term, the dollar would appreciate by an amount such that the appreciation plus the Canadian real interest rate would approximate the U.S. real interest rate.

Those who oppose such a move fear that the initial shock to import and export prices from depreciation would translate into a continuing and growing disparity between Canadian and American inflation rates, leading eventually to higher nominal and real interest rates as we slide down the slippery slope of depreciation. Our work suggests this is not a major threat. Simulations with lower nominal interest rates in Canada do indeed lead to an initial depreciation, but this is followed by subsequent appreciation. The initial external price shock gives way to more regulated prices, and the improved

productivity associated with operating the economy closer to capacity. This is, of course, a judgment call, but we are quite prepared to put our judgments on the table.

Are there other reasons for pursuing a more independent monetary policy? Even if we were at full employment today, would we want to reduce nominal and real interest rates? There are at least two additional reasons that lower rates are desirable. If real interest rates exceed the real growth of the economy, this implies a growing share of income to rentiers. In the same way, growth in real wages that exceeds growth in the economy implies a larger share to labour. In the long run, stability in our social structure requires some stability in income shares, although the levels at which those shares stabilize is the result of the relative bargaining power of various groups. But as long as real interest rates exceed the real growth of the economy, there will be a continuous redistribution of income from debtors to lenders.

In the case of the primary government deficit, the debt-GNP ratio will inexorably rise as long as real interest rates exceed growth in the economy. (The primary deficit is the deficit excluding interest payments.) But the instability is also there for private debtors, unless they can run primary surpluses on a continuing basis. Internationally, as well, less developed countries must run surpluses on merchandise account to offset the instability associated with real interest rates exceeding their export growth. The flip side of this is that assets-to-GNP ratios will also continue to rise as long as real interest rates exceed real economic growth. Overall, at some time in the not-too-distant future, it would be desirable to stabilize income shares and remove the inherent instability associated with rising debt and asset ratios.

A second reason for lower interest rates, especially at full employment, would be to twist our allocation of resources towards an increased share of investment in GNP. This would ensure that the potential growth of the economy is maximized, and also that real incomes per capita are maximized in the longer run. At full employment, the instability of lower interest rates could be offset by a move to more fiscal restraint, in order to avoid the excess inflation that occurred in the early 1970s.

But why are we arguing for an independent Canadian monetary policy? Would it not be better if U.S. interest rates simply declined further? Clearly, the answer to this is yes. Lower real interest rates in the U.S. would stabilize their debt-GNP ratio, and bring more economic growth. This would of course help Canada, given our close linkages to the U.S. economy. Lower U.S. interest rates should also help expand their productive capacity, preventing a return of inflation, and would likely lead to further depreciation of the U.S. dollar against the currencies of its major trading partners. This would allow for lower interest rates in Canada and improve our international competitiveness.

Yet there are also limits to the degree of independence the U.S. can pursue in its monetary policy. Higher real interest rates at this point would threaten the international financial system, particularly the likely repudiation of debt by less-developed countries. The U.S. banking system would come under substantial pressure from bankruptcies in agriculture and other over-extended sectors. Higher interest rates would also appreciate the U.S. dollar against other currencies, leading to deeper difficulties for U.S. manufacturing and a larger trade deficit.

High real interest rates are often said to follow the trend of U.S. government deficits. This may be the case, but it has yet to be proven. A more reasonable framework is to recognize that a game of "chicken" has been going on between the Federal Reserve, the Executive Branch, and Congress. Retired Reserve Board Chair Volcker routinely insisted on reductions in government deficits before promising lower real interest rates. Congress and the President have fought over changes in fiscal policy, and both resent the obstinacy of the Fed. Lower nominal rates would show that it is quite possible for U.S. interest rates to decline in real terms, and quickly. But when will they stop playing games?

To some extent, Canada abetted Volcker in his game of chicken. As the U.S.' largest trading partner, we did not react to the high real interest rates in the U.S. Our failure to depreciate our currency through lower interest rates reduced the external pressure on the U.S. for lower rates. This is perhaps another reason why we should pursue a more independent monetary policy in Canada. Clearly if they have an inappropriate monetary policy it makes no sense for us to follow them.

How should interest rates be set if Canada wishes to pursue a more independent monetary policy? The basic target for short-term treasury bills should be a real interest rate of three per cent, plus or minus one percentage point. This is a good estimate of the potential growth rate of the Canadian economy, with about 1.5 growth in the labour force and productivity growth of a further 1.5 per cent. With inflation currently running between three and four per cent, this would imply short-term interest rates in the range of six to seven per cent. With current treasury bill rates close to nine per cent, this would mean a drop in short-term interest rates of at least 200 basis points.

There may be skepticism about the Bank of Canada's ability to lower interest rates by 200 basis points. But if it is made clear that a real interest rate rule is the basis for setting short-term interest rates, it will take market participants less than a week to realize that they can make money by believing that rule. Their stabilizing speculation will maintain real rates around the three per cent, without requiring mammoth open-market operations by the Bank of Canada.

Of course, the market needs to know what real interest rates are. If the federal government issued real interest rate bonds with several maturity dates as part of the package, there would be a daily market signal to guide the

conduct of monetary policy and of market participants. This could also lead to a reduction in the cost of carrying the deficit and would create an attractive asset for pension funds, life insurance companies, and ordinary Canadians planning for their retirement.

At the same time, market participants must be told that the exchange rate is flexible, both upward and downward. In the very short term, the exchange rate may well be dominated by interest rate movements, but the relationship is a much more complex one. In the course of a year or longer, the exchange rate is also influenced by relative price performance, relative economic growth, the current account balance, and the ephemeral international confidence. But participants in international trade and finance are much better equipped to handle fluctuations in exchange rates than are most Canadians to handle highly variable interest rates.

The third part of the package would be to maximize the benefits from lower interest rates and the possible initial drop in the exchange rate, by minimizing the initial price shock and any subsequent inflationary reactions to it. Such an effort would benefit from some form of voluntary incomes policy, deregulation of some key sectors, and perhaps even a move towards freer trade.

If we adopt this course in monetary policy, we must also be prepared to stabilize our maximum real interest rates. If there is a substantial drop in nominal U.S. rates or an inflationary burst that drives their real rates below Canada's we should live with the consequences. The latitude of plus or minus one per cent for real rates is purposely narrow, to limit major deviations from longer-term objectives.

The move to a more independent monetary policy is not without risk. We should be especially concerned if the changeover increases inflation without improving real economic growth or reducing unemployment. In this case, we should be prepared to curtail inflation, but not through a return to restrictive monetary policy.

There are also some things we should not do in adopting a more independent monetary policy. In particular, with the official unemployment rate close to the double-digit range, further fiscal restraint is neither necessary nor desirable. Lower interest rates would serve to dampen consumer incomes, by reducing interest earnings from government and other sources. This will "automatically" improve federal government balances and weaken real disposable incomes. With some initial depreciation, real incomes are also weakened by the initial price shock. A move to lower interest rates will automatically move the fiscal posture towards more restraint!

In order for this independent monetary policy to work, we cannot resist the depreciation or appreciation of the currency. Nor should we adopt exchange controls to minimize these movements. This represents a major break from past policy, but that may be a good thing given the track record.

Finally, while it may be tempting to move only gradually in the direction of a more independent monetary policy, the last ten years of fiscal and monetary policy seem to show that gradualism is not the way to go. A more gradual approach leaves people wondering whether you are serious about the move, and further postpones the benefits of stronger economic growth.

What should be expected from a reduction of short-term interest rates by 200 basis points? The initial depreciation of the Canadian dollar against the U.S. dollar would be slightly less than four per cent, with subsequent appreciation of about one per cent per year. At current exchange rates, this would mean about three cents U.S., or a drop in the exchange rate from say 76 cents to 73 cents. The initial impact would show up in a one per cent increase in the consumer price index. After the first year, there would be less inflation, as appreciation reverses or begins to reverse the initial depreciation and lower nominal interest rates result in lower regulated prices. Productivity gains would also contribute to lower inflation. Improved economic growth in the first year (+0.5 per cent) would be led by increased exports (0.4 per cent), import substitution (-2.5 per cent), and residential construction (+5 per cent), with subsequent improvements to over one per cent after three years due to business investment. Improvements in the unemployment rate throughout the first five years range from an initial 0.1 per cent to 0.5 per cent.

Federal government balances improve by $6 billion in the first year, due to lower interest payments and increased economic activity. Some or all of this gain can certainly be recycled to the consumer through tax cuts or targeted expenditures on jobs, to speed up the return to full employment.

It is interesting to note that the Canadian economy is better off in all dimensions. There is less inflation, lower unemployment, more economic growth, higher productivity, improved government balances, and an improved current account balance. There is also more room for governments to manoeuvre.

Although an econometric simulation can provide precise estimates of the effect of lowering short-term interest rates, there is much dispute about the accuracy of such estimates. All models are an incomplete approximation to reality. Other models may show larger or smaller effects for a given change. But some models do at least show positive effects from a more independent monetary policy!

It is equally important to understand that an independent monetary policy represented by a reduction in interest rates by 200 basis points is not sufficient to quickly return the Canadian economy to full employment. The gap in output is reduced by some $5 billion to $7 billion in 1985 dollars. That is, instead of leaving $50 billion on the table each year, we are only leaving about $45 billion as a result of this policy. Certainly, the challenge is to do even better. But a more independent monetary policy can contribute to such an improvement.

Refusing to consider such a policy leaves us in a situation where stability in the federal debt-GNP ratio can only be achieved through further fiscal restraint in support of a primary surplus. The likelihood of such a policy returning us to full employment is extremely low!

DISCUSSANTS

Patrick Grady — Grady Economics

Michael McCracken is one of Canada's leading economists of an activist Keynesian persuasion. Relative to the rest of the economics profession, he places much greater emphasis on reducing unemployment quickly from levels that are generally agreed to be unacceptably high, and less weight on restraining inflation.

If any Canadian economist can be expected to answer a hearty yes to the central question, whether macro-economic policy can reduce unemployment, it is Mike McCracken. It is thus particularly significant that he has provided us with a weak and qualified yes.

In his paper, Mr. McCracken says a drop in real interest rates of at least two percentage points would reduce unemployment by an initial 0.1 to 0.5 per cent over five years. By itself, this would constitute a significant but not dramatic improvement in the unemployment rate — so much for monetary policy. Undoubtedly, these proposals for relatively modest improvements are not what many of you would like to hear. But if other leading Canadian macroeconomists had been here this morning, their views of macro-economic policy as a tool for reducing unemployment would have been even weaker and more qualified.

The fact is that we macro-economists are a much more humble lot than we were 20 years ago. After starting from a belief that higher inflation could be traded off for lower unemployment through expansionary monetary and fiscal policies, we have learned that inflation has a way of continuously spiraling and eroding the temporary benefits of lower unemployment, until restrictive policies are triggered and unemployment soars. Experience has taught us that there is no long-run trade-off between inflation and unemployment. Instead, there is a natural, Non-Accelerating Inflation Rate of Unemployment (NAIRU), which is consistent with steady inflation and tends to re-establish itself on its own. The Macdonald Commission estimated this rate in the 6.5 per cent to eight per cent range.

Canadians have been forced to pay an extremely high price in unemployment to bring inflation under control. Established theory suggests a strong tendency for the unemployment rate to decline to the natural rate on its own, so prudence would seem to dictate a fair degree of caution in setting fiscal and monetary policies.

In my view, this is more or less what the government is doing with its present monetary and fiscal policy. Fiscal policy emphasizes tax increases and expenditure cuts designed to reduce the deficit and stabilize the increase in the ratio of government debt to GNP. There is much room for disagreement about specific tax increases and spending cuts, but the broad thrust of current

fiscal policy is in line with the recommendations of the Macdonald Commission, and of the Economic Council of Canada in its 1985 Annual Review, *Strengthening Growth*.

Monetary policy is being conducted to ensure that the recent progress against inflation is maintained. Lower interest rates have been accepted, as inflation and U.S. interest rates have come down. Interest rates may not be coming down as fast as some would like, but we have come a long way in that direction over the last few years without jeopardizing the reduction in inflation.

Like all other Canadians, including the Governor of the Bank of Canada, I share the desire to see interest rates lowered. In the abstract, I think a target of three per cent plus or minus one is in the right ballpark for real short-term interest rates. If U.S. interest rates were to come down to that range and inflation were to remain moderate, it would be appropriate for Canadian interest rates to fall in the same range.

However, if U.S. real rates stay high, it is not clear to me that we have the option of unilaterally lowering our real short-term rates to this target range. In support of my skepticism, I quote from the current Canadian economic scripture, the report of Macdonald Commission. The quote, of course, comes from a different page than that cited by Mr. McCracken in support of his own proposal. The parallel between the Macdonald Commission and Holy Writ is very close, as you can see.

The Macdonald Commission report (vol. 2, p. 328-329) asks what scope Canadian authorities have "for insulating the domestic economy from interest rate levels that are too high to be compatible" with national economic goals? Its answer is not very encouraging for those that would like to see a unilateral reduction in Canadian interest rates. The Macdonald Commission concludes that:

> "One of the most striking developments of the last 20 years has been the internationalization of capital markets. Nowadays, the level of real interest rates is determined primarily by the world-wide interaction of the supply and demand for capital...As long as we permit capital to flow across our borders with almost complete freedom, the level of real interest rates prevailing in the world economy will be a major influence on our rates, especially in the longer run...To specify the "longer run" is important because the Canadian authorities do have some short-run influence over domestic real interest rates as long as they maintain flexible exchange rates...there is a short-term trade-off between the domestic level of real interest rates and the exchange rate...A temporary depreciation of the currency can stave off temporary increases in world interest rates or delay the effects of more permanent increases. It cannot stave off the latter forever. In the long run — and that period is sometimes better measured in months than in years — real interest rates in Canada are broadly determined in world markets."

Table 1 shows that nominal short-term interest rates in Canada have typically averaged higher than those in the United States (0.7 per cent from 1951 to 1984, 1.1 per cent from 1970 to 1984, and 1.9 per cent from 1980 to 1984). The main exception was in the early 1970s, when inflation was getting out of control in Canada.

Table 1

SHORT-TERM INTEREST GAP: CANADA-US

1951-1984

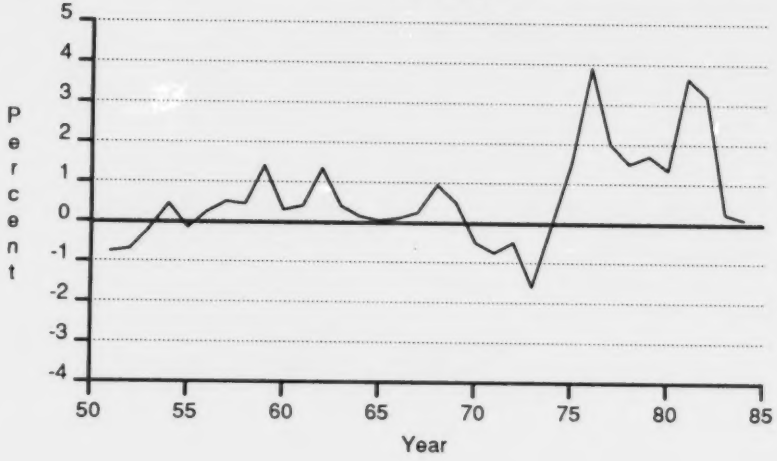
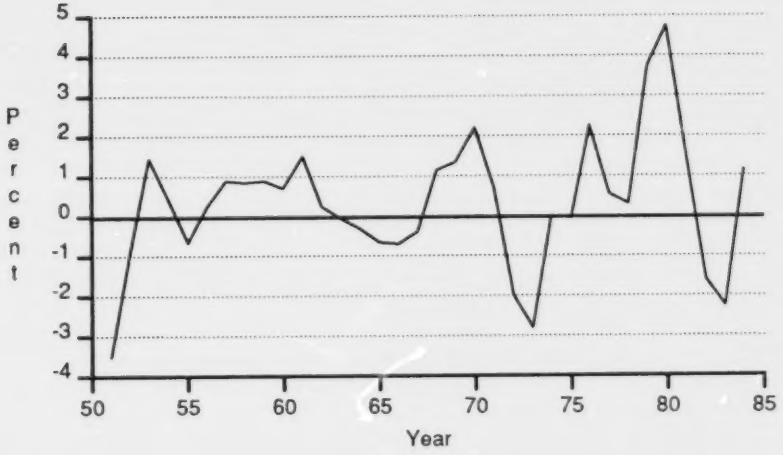


Table 2 shows that real interest rates in Canada have also been higher than in the United States (0.3 per cent from 1951 to 1984, 1.1 per cent from 1970 to 1980, and 0.7 per cent from 1980 to 1984). Real short-term rates only fell below the U.S. for a few years in the 1960s, in 1972 and 1973, and in 1982 and 1983. The years 1972 and 1973 were marked by deteriorating inflation performance in Canada relative to the U.S. while 1982 and 1983 saw inflation yield to restraint much more slowly in Canada than in the U.S. None of this offers much promise of maintaining Canadian short-term interest rates below those in the U.S. for any length of time in an non-inflationary environment.

As for the "game of chicken" between U.S. Federal Reserve Chairman Volcker, Congress, and the President, I do not believe Volcker was just playing games in trying to encourage the Administration and Congress to cut the deficit in return for monetary ease. The unemployment rate in the U.S. has been close to seven per cent, and the U.S. economy is operating in a range where a trade-off of fiscal restraint for monetary loosening may help sustain growth in output and employment without a re-emergence of inflationary

Table 2

REAL INTEREST GAP: CANADA-US
1951-1984



pressures. This is quite different from the situation in Canada, where unemployment is close to 10 per cent and there is little risk of demand pressure pushing inflation up. We should not judge U.S. policy by what would be best for Canada, but on the basis of what makes the most sense from a domestic point of view.

Finally, Mr. McCracken estimates that a reduction in short-term interest rates would initially raise the consumer price index by one per cent, but that the CPI would be lower in the longer term because of productivity improvements, decreases in regulated prices, and the subsequent appreciation of the dollar. Most other models would not produce such an estimate. It is hard to believe that a more expansionary monetary policy will not raise inflation.

Sidney Ingerman—McGill University

In the macro-economy as we find it today, we are confronted with a situation where we have had double-digit unemployment, somewhere between 1.4 million and two million unemployed, depending on how you measure unemployment; where the number of long-term unemployed in outlying regions of the country is getting frighteningly high; where food banks and bread lines are a daily reality; and where there are increasing numbers of homeless

people in our urban centres. In Ottawa, a city of relative prosperity, *most* of the advice economists are giving government is dangerous — reduce deficits by cutting government spending — and the *"best"* advice — gently increase the money supply — offers little or no hope for improvement in the economy. Worst of all, one of the key questions of macro-economic policy is given short shrift, that is, the question of income distribution. How is income being distributed? What is the effect on income distribution of the macro-economic policies that we do have? I believe that the negative effect of current macro-economic policies on income distribution makes them socially unacceptable and economically mistaken.

A lot of the discussion, certainly the discussion about inflation, resembles a cat chasing its tail: fight inflation to lower unemployment; lower unemployment will cause inflation. Such a discussion takes us nowhere. We came through a period of stagflation during the 1970s and into 1980. There is a fair amount of agreement that events in the Middle East contributed to a massive inflationary experience. But now that the worst aspects of that experience are past, the inflation rate in Canada, the U.S., and in most of the developed world is not a pressing problem. We still hear people saying inflation is a threat hiding behind the door, but I would like to see evidence of that. I do not hear any *theory* of inflation, except that reduced unemployment will lead to runaway, accelerating inflation. I do not see much evidence for this view, empirical or otherwise.

Furthermore, Diane Bellemare has shown that although there are certain structural differences between Sweden, Austria and Canada, vigorous macro-economic policy has been effective in the former countries and can be effective here. This is true despite the complicated situation we have inherited, where banks and other financial institutions acted speculatively, manipulatively, and irresponsibly in the 1970s, and contributed to the instability that is part of our inherited economic problem.

Every macro theorist, economist and socially concerned person must now direct their attention to ways of promoting economic growth. This involves promoting an equitable, socially acceptable, and humane distribution of income. Everything that has happened in economic policy in recent years has contributed to a maldistribution of income, and this maldistribution of income now makes it more difficult to promote economic growth and reduce unemployment. Even in the unionized sector of the economy, there has been a massive deceleration of wage increases. High unemployment coupled with anti-inflation boards, wage controls, and unfriendly government policies at the federal and provincial levels weakened the ability of organized labour and other workers to keep up with increases in productivity, however low they may have been. This has contributed to weakness on the consumption side, and it will make recovery of any sort far more difficult.

One of the characteristics of the tax and spending policies of recent federal governments has been to put the tax burden on the middle class and ease

taxes for the rich, thus creating a situation where savings are increased and consumption is weakened. Under these circumstances it is not surprising to see high Canadian savings rates accompanied by a large deficit. Such a deficit is necessary, in light of saving rates, to maintain even the poor employment situation that currently exists.

Economists and the governments they advise seem to have generally accepted that there will be a high level of unemployment even when the economy is functioning properly. This reflects the practice of taking data which are weak, using equations that are questionable, and then projecting forward into a distant future about which we know less than nothing. (We hardly know what is likely to happen sixty days from now, and we know even less about the next five years.) On this basis we are told that the lowest possible level of unemployment in the foreseeable future is something like seven per cent.

Even if we accept this figure, we are still at close to 10 per cent unemployment. If the so-called natural rate of unemployment is seven per cent, there is still room for expansionary policy: movement should be made between the current rate and the questionable natural rate. I do not see any evidence of policies to close that gap. Let us test at least that theory; let us use expansionary fiscal and monetary policies. If inflation shows up, we can back off. I do not think we need a wildly expansionary policy, but the current "wisdom" is that *nothing* can be done. Doing nothing means deficits get worse. Doing nothing means human suffering will get worse. Doing nothing means we will have an unsatisfactory society.

The so-called natural rate of unemployment is there to warn us that if we do something, we are going to get accelerating inflation. Again, on what theory is this based? I do not see any clear theory. I see a proliferation of equations and regressions. I do not see any indication that inflation is currently a threat.

Mr. McCracken is an activist who wants to use government; among today's economists, that is progress. He seems to be saying, perhaps for purposes of illustration, that the natural rate of unemployment is about five per cent. If that is the case, I would like to hear some comment on why he differs from the majority view about the magnitude of the "natural" rate of unemployment. Mr. McCracken advocates an active and independent monetary policy, says we may have to take out an anti-inflation insurance policy to support such measures, and talks about voluntary incomes policy, even though we do not have a good track record with voluntary or involuntary incomes policies in this country. He talks about deregulation; again I wonder if this is the way to go. Finally, it seems to me that freer trade and his independent monetary policy may be fundamentally contradictory. I conclude by suggesting that theoretically, technically, and in policy matters, we are failing to cope with the very serious and fundamental macro-economic problems we face today.

David Dodge — Senior Assistant Deputy Minister (Taxation), Department of Finance

It's really important that we keep before us the policy problem of full employment because, although we may have very different views on how we get from where we are to where we want to be, I think we can all agree that we do indeed want to get there. I think the interesting thing is that, if this symposium had been held 10 or 15 years ago, the nature of the topic would have been quite different. I note that the title for the session is "Can Macro-Economic Policy Reduce Unemployment?"; ten or 15 years ago, we would have been debating *how*. I think also you should recognize that you do not have anything like a representative group from the profession in this section. In one way or another, we are all to some degree of the Keynesian persuasion, some more than others. I guess in this group, I feel a bit like Wendy Dobson, the former director of the C.D. Howe Institute, having normally been on the Keynesian end of things, and now being called upon to contribute less than the total Keynesian view to the discussion.

Nevertheless, let me start right off by saying that most analysts within the Department of Finance, clearly believe that macro-economic policy does have a role to play in trying to reduce current rates of unemployment. The problem is how to play, given the limited room that there is to play with.

While fiscal and monetary policy appear to operate on two very different planes, they are in fact two sides of the same coin. Indeed, one might spell that word C-O-Y-N-E for anybody that was in this town 25 years ago, because in many ways the debate on macro policy that we are having today is not a debate so much of more or less, but rather of how to conduct that policy and what balance there ought to be between the fiscal and monetary sides. And I think that on balance, the dominant view in the economics profession — certainly in the Macdonald Report, which is not a bad representation of the mainline thinking of the profession — is that we have probably tipped the thing the wrong way, that we have tried to put in too much fiscal stimulus and probably not enough on the monetary side. But there really is a link between these two that is extremely important to recognize.

Michael McCracken, in his paper, talked about monetary policy as if there were not another arm of policy on the fiscal side. He also talked about trying to get real interest rates at the short end down to two or three per cent. Presumably that still means real rates at the long end up around four per cent or so, which is above Canada's potential rate of growth. The question is whether you can do what Mike McCracken wants to do without moving in the opposite way on the fiscal side. That is in many ways the real question before us. Indeed, if we want some degree of independence in monetary policy — and the Governor of the Bank of Canada and everybody else in this town would love to have some degree of independence on monetary policy — if we want it, how do we get it? Mr. McCracken seems to suggest that we can get it by simply moving ahead as if we had it and things will tend to

work out — that we will not get inflationary consequences, that we will, get a decline in interest rates by increasing the money supply. Unfortunately, for a lot of technical reasons and because of the way markets work, we have not been very successful when we have tried that in the past. Indeed, the last time we tried it, we got an upward movement in interest rates.

So you can't reduce interest rates by putting in monetary expansion and hoping you will end up getting there. You probably need some degree of monetary independence to get interest rates down. If everybody out there — Canadians and everybody else — believes there is some potential strength in the Canadian dollar relative to the rest of the world's currencies, they will be willing to hold the Canadian dollar at a lower rate than a U.S. security, hoping to get some appreciation that will compensate for a lower rate of return.

The problem is that very few people, including most Canadians that are looking at holding assets, really believe that we will conduct policy in a way that contributes to the appreciation of the Canadian dollar. Some countries have attained a degree of independence, not that we would necessarily want to follow them. The Swiss had the great advantage of keeping their unemployment rate low by kicking 20 per cent of the labour force out of the country. I do not think we would want to emulate that particular example, but countries such as Germany, and more recently Denmark, have made room for some independence on the monetary side by becoming modestly restrictive (in Germany's case highly restrictive) on the fiscal side. This has given them some room to manoeuvre, if you will, on the monetary side.

Why is it better to tighten up a bit on the fiscal side to get some room to manoeuvre on the monetary side? I think that is the interesting question. In Canadian terms, all segments of the nation are highly sensitive to interest rates. We do not allow deductability of interest for consumers, hence consumers have shown they are very sensitive to interest rates. When interest rates go up, their savings rates go up. If we can pull interest rates down there is some reasonable presumption that we will get a decline in the personal savings rate, and an increase in household consumption that will be very important in fueling domestic growth. The results over the last quarters of 1985 gave some indication that this may be the case. Second, since our industry is much more capital-intensive than south of the border, it is more sensitive to interest rates. If we can get those rates down, our investment picture is likely to brighten. Third, the cost of servicing the debt of the Government of Canada is highly sensitive to interest rates. A reduction in interest rates of 100 basis points over four years would save us roughly $4 billion annually in federal government interest payments. When you divide that among 25 million people in the country, it's a lot of money for each and every individual Canadian.

But in order to give the Bank of Canada some degree of independence, we must do better on the fiscal side by reducing the deficit. It is not going to be

very easy, and there are better and worse ways to go about bringing that deficit down. It's not going to be easy, as we all know, but it is important to note that there is an inter-relationship between fiscal and monetary policy, an inter-relationship that Mr. McCracken's paper does not focus on. Based on our own models, it appears preferable to create more room to manoeuvre on interest rates by trying to show a better balance on the fiscal side of the house.

Intervening in the Labour Market: Which Way to Go?

No subject in economics is more likely to bring forth disagreement about policy recommendations than discussion of the labour market. To start, with there are serious objections to applying the market metaphor to human labour. Contributors to this section do not mince words in their discussion of the sort of policy proposals that are being tried or are under active consideration in Canada.

Tim Hazledine outlines the case for price controls. In an economic environment where the fear of inflation has led mainstream economists to drastically revise full employment targets, to the point where they would leave as many as a million Canadians out of work if they were fulfilled, his alternative merits close attention. His examination, one of the few thorough examinations of this important policy option, draws on his recent book, *Full Employment Without Inflation*. His position is clear: the principal reason for unemployment is a shortage of jobs.

Frank Reid prefaces his careful exposition of current options for employment-sharing with a telling explanation of how "externalities" affect employment as a contract between a worker and an employer. Simply put, those who are not a party to the transaction may have legitimate interests that are ignored. Reid is well aware of the difficulties involved in introducing programs to reduce work time, share jobs, or compensate workers for the introduction of short time in the workplace, but these difficulties are brought into focus in the discussion of his article. If anything, Arthur Donner and Mel Kliman elicit even more critical comment in their discussion of wage subsidies. Youth employment initiatives offered by Employment and Immigration Canada, and other workfare programs introduced on a voluntary basis by some provinces, continue to raise ire.

In her comments, Monica Townson is very clear about her objections. The programs under discussion are modelled to meet the employment needs of prime age males, and often ignore women's job concerns entirely. In her view, wage subsidies should be set aside. Work sharing makes sense when legislated reductions of the work week are introduced, but only when workers do not have to give up income in order to qualify. Townson notes that the impact of work time reductions is usually borne by lower income workers.

Keith Newton points out that more Canadian experience with labour market adjustments is now available and that not all of it is encouraging. Many wage subsidy programs seem to provide a large windfall gain to employers rather than create new jobs. This problem must obviously be addressed before future programs are designed.

Terry Hunsley has considerable problems discussing the labour market in terms of rigidities. He would like to see a better quality of life more evenly distributed among Canadians, but suggests much of the discussion of labour market intervention lacks a clear statement of objectives. Hunsley has trouble accepting that a government committed to job creation would lay off workers. He sees little prospect for private sector job creation, and thus favours public sector intervention. But not all public policies are equal in distributing benefits where they are needed.

VII

PRICE CONTROLS FOR FULL EMPLOYMENT

Tim Hazledine
University of British Columbia

Introduction

This paper reassesses an apparently old-fashioned and discredited economic policy — direct price controls — in light of recent developments in economics. It turns out that price controls can be seen as an example of the most modern of concepts — a "regime shift" — that would generate quite a radical change in the rules of the game played by participants in the economy. The result of these changes would be a really worthwhile improvement in the capacity of the system to deliver lower unemployment without inflation.

This proposal combines the theoretical notion of a regime shift with another powerful development in economics — the increasingly widespread realization by micro-economists that the bulk of economic activity does not take place in perfectly competitive markets. Specifically, most sellers of goods and services are "price-makers", not "price-takers". The price control proposal amounts, in effect, to *imposing* price-taking behaviour, by shifting the market regime under which firms set prices from monopoly or oligopoly to quasi-perfect competition, with beneficial implications for employment and inflation.

Any proposal to radically reduce unemployment must establish that such a change would be technically feasible, in the sense that the economy would be capable of functioning efficiently without a substantial "pool" of unemployed workers. This issue is dealt with in section 2, which provides a detailed

repudiation of the various rationalizations of unemployment offered by orthodox "neo-classical" macro-economics. Basically, faced with an apparent discrepancy between the facts of mass unemployment and the theory of a perfectly competitive market system, neo-classicists (of both monetarist and Keynesian variants) have chosen to twist the facts to fit the theory.

Section 3 suggests how the theory might be altered to accommodate the facts, sketching an explanation of persistent unemployment as a natural consequence of our low-elasticity, oligopolistic economies.

Section 4 introduces the idea of the regime shift needed to effect any dramatic improvement in the situation, and section 5 gives details of the policy instrument proposed to achieve this — a system of high-level price ceiling controls.

Section 6 attempts to counter a number of charges that are commonly, though usually casually, tossed up against price controls, and section 7 concludes the paper. Throughout, only very recent sources are footnoted. For documentation of other points, the interested reader is urged to consult my book, *Full Employment Without Inflation*, especially Parts I and III.

The Feasibility of Full Employment

For four decades, the research agenda of neo-classical macro-economics has centred on the issue of "stabilization policy" — that is, the attempt by economists to supply governments with the policy tools that will enable them to smooth out the swings of economic activity between recession and boom. To put it crudely, but without caricature, orthodox economists have been divided into two camps. The Keynesians believe successful stabilization policy to be demonstrably feasible. The new classicists formerly monetarists, insist that governments' meddling, well-meaning or not, is likely to do more harm than good, and may actually exacerbate the fluctuations in GNP and employment that fiscal and monetary policies are supposed to suppress.

What has only become apparent in the last ten years or so is that the debate over stabilization policy, though not irrelevant or unimportant, has really become of secondary importance. In the period since the Second World War, the year-to-year or cyclical swings in economic performance have been increasingly overshadowed by a remorseless upward trend in unemployment.

Table VII-1 demonstrates that for each of the major Keynesian economies — Canada, the U.K. and the U.S. — average unemployment over five-year periods has shown an upward trend beginning at least two decades ago.

The cumulative effect is such that even after an unusually strong recovery from the savage recession of 1982, unemployment rates in all three economies remain well above those recorded at the troughs of the worst recessions of the 1950s and 1960s.

Table VII-1

Economic Performance: Five Year Averages

	1951-55	'56-60	'61-65	'66-70	'71-75	'76-80	'81-85
Canada							
Unemployment Rate	3.5	5.6	5.4	4.6	6.1	7.7	10.4
Inflation Rate	2.6	1.9	1.5	3.7	7.1	9.0	7.4
U.S.							
Unemployment Rate	3.9	5.3	5.5	3.9	6.1	6.7	8.3
Inflation Rate	2.2	1.8	1.3	4.3	6.8	8.9	5.4
U.K.							
Unemployment Rate	1.4	1.7	1.8	2.2	3.2	5.5	12.0
Inflation Rate	5.6	2.6	3.5	4.5	12.9	14.4	7.1

Source: OECD. *Main Economic Indicators*, various issues.

How is it that this alarming event has not become the main preoccupation of economics? Again, to put the matter crudely but without caricature, mainstream economists have dealt with increasing mass unemployment by *denying its existence*. Specifically, it is proposed that most of what the lay public simplistically labels as unemployment is actually leisure, voluntary and efficient job-search activity, or the consequence of the necessary and desirable redeployment of workers in an ever-changing job market.

None of these rationalizations has reasonable empirical support. Although huge numbers of adults have voluntarily left the labour force (mostly being educated, rearing families, or retired), there has never been more than anecdotal evidence that significant numbers of those registered as without work but actively seeking it — i.e., the officially unemployed — are in fact swindlers who are secretly enjoying their idleness.

The voluntary search argument is more subtle. The idea here is that workers choose to invest time in full-time job search, to find a better job. Loss of current income through unemployment is traded off against the higher income eventually achieved.

It is fair to say that the cumulative weight of empirical research leans overwhelmingly against the search model as a reasonable explanation of mass unemployment.[1] The trouble is that, whereas searching while unemployed is certainly one way of getting a new job, looking around while already employed is nearly always much better — you get paid a full wage while searching. If the search is unsuccessful, the present job can be quietly continued with nobody the wiser. Being currently employed may make the worker more attractive to a prospective employer — it at least demonstrates employability. Certainly, most academic economists do their best to change jobs without an intervening spell on the unemployment register. Most unemployed people (including new entrants to the labour force) accept the first job they are offered, rather than "sampling" offers as presumed by search theorists. Search itself typically takes only a few hours a week — hardly a full-time activity. Most unemployment is relatively long-term, and often ends in discouraged departure from the labour force, rather than a new and better job. And, most damning, search-on-the-job actually results, on average, in *higher* wage increases than search from unemployment.

Related to the job-search model are attempts to explain unemployment by various demographic and social policy shifts. In the early 1970s it was quite popular to link rising unemployment to increases in unemployment benefits, minimum wages, and in the supply of young and female workers. Higher benefits, for example, could induce a rational job searcher to search longer and more thoroughly before choosing among the multitude of available job offers.

A problem with these explanations is that the paths of benefits, minimum wages and demographics all *changed direction* in the mid to late 1970s, while unemployment remained on its unremitting upward trend. The earlier correlation was either accidental, or too unimportant to compensate for the larger forces that dominate unemployment.[2]

The big fallacy of all supply-side (i.e. blame-it-on-the-worker) rationalizations of unemployment, with the possible exception of the minimum wage argument, is that they beg the central question. Certainly, youth and women have higher average unemployment rates, so that an increase in their share of the labour force goes along with an increase in the total unemployment rate. But this doesn't *explain* or justify higher aggregate unemployment, because it doesn't explain why women and young people are more likely to be unemployed to start with. Only if these groups choose to remain unemployed longer — presumably due to some quirk in the labour market that makes it profitable for them to search longer and/or more often than adult men — can their increased share of the labour force be used to *justify* higher total unemployment. Such dependence on voluntary job-search arguments is, as shown above, wholly implausible.

To summarize, supply-side factors may have some (though probably small) empirical validity in explaining the average duration of unemployment. But

they do not plausibly tell us how the workers become unemployed in the first place, and so fail to offer a reasonable rationalization of mass unemployment.

For this we must turn to the other side of the market — the *demand* for workers. If it is not workers unwilling to work that causes unemployment, it must be a lack of employers willing to offer work.

One demand-side explanation that has been around for a long time is the "structural unemployment" argument. Because product markets and technologies are continually changing, so too will be the type and location of available jobs. As a result, some workers will always be unemployed while relocating and/or retraining, and the numbers will go up in periods of unusually turbulent structural change.

The structuralist model has recently benefited from a revival of research interest,[3] and it cannot be dismissed as easily as voluntary search and other supply-side stories. However, it does not provide an adequate explanation of our present predicament.

The problem comes in reconciling the model with the long periods in history when rapid structural change coexisted with what now seem like desperately desirable levels of near-full employment. For example, during the long post-war expansion through the 1950s and 1960s, employment in agriculture in Canada fell from around 20 per cent of the labour force to less than five per cent. This enormous structural change — involving radical shifts in the location and type of jobs for the people involved — was accomplished quite smoothly and without mass unemployment.

The key point is that while the closing of a steel mill, say, results in people losing their jobs, the closure is not the cause of unemployment. It is normal and desirable for some industries and occupations to be in decline at any time. Difficulties arise when other industries and occupations do not expand quickly enough to take up the displaced workers efficiently. In periods and countries where expansion has matched contraction, structural unemployment has not been a major problem.

It is the total or aggregate demand for labour that is lacking — the availability of a widespread range of employment opportunities that would enable the normal process of frictional or structural adjustments to go on without causing mass employment. To put it succintly, unemployment is caused by a lack of jobs. We examine the reason for this in the next section.

The Real Reason for Unemployment: Not Enough Jobs

Having rejected the commonly advanced rationalizations for mass unemployment, we must come up with a viable alternative. Mine sound simple enough: unemployment is the result of an overall shortage of jobs, which causes the total demand for labour to fall short of the able and willing supply of workers.

To the non-economist this may sound obvious to the point of truism, but in fact two difficult questions must be answered before a lack-of-jobs model can be accepted. It is necessary to explain why the market hasn't corrected the imbalance through the necessary wage and price changes, and, why the best efforts of activist Keynesian governments have been insufficient to eliminate unemployment through expansionary fiscal and monetary policies.

The quick answer is that market and policy have both failed because the structure of the economy renders such remedies ineffective. Specifically, our economy is now dominated by "oligopolies" big firms competing carefully with each other which do not respond properly to wage flexibility or to expansionary government policies.

The key concept is that of "elasticity" — our measure of the responsiveness of the system to changes in important variables. The perfectly competitive world assumed in neo-classical economics is highly elastic, at least with respect to changes in prices and wages. Specifically, if offered a wage cut, the small firms that make up the neo-classical system should respond enthusiastically with increases in employment. These firms don't have to worry too much about being able to sell what they produce — there will always be room for it in the relatively vast market in which they operate. Their output, and thus employment, is determined by supply, and in particular, by their costs, which are, of course, greatly dependent on the wages they pay.

The first, most optimistic, generation of Keynesians believed that shifts in aggregate demand engineered by monetary and fiscal policy should get a large (elastic) response in output and employment, and have little or no effect on prices.

The unfortunate failure of the economy to behave in this way was blamed, like the existence of unemployment, on failings in the labour market, rather than the underlying faith in perfect competition.

But this faith is wildly discordant with the facts. Most markets in the modern economy, in manufacturing and in services, are dominated by a few, and thus relatively large sellers, whose responses to economic variables are quite different from those of the mythical perfect competitor.

Specifically, employment responds inelastically to both wage cuts and aggregate demand policy in an oligopolistic economy. By offering a wage cut, workers or their unions hope to induce their employers to cut prices, sell more, and take on more labour in a trade-off of more jobs for less pay per job.

Unfortunately, the terms of this trade-off are not attractive in an oligopolistic economy. It appears that oligopolists generally expect an inelastic response to price cuts, implying that, in percentage terms, the cut in pay would exceed the increase in jobs, so that workers as a group (i.e., previously unemployed plus previously employed) would be worse off. This is because firms are conscious of their size relative both to the total market (which limits the room for further expansion) and to other large firms (which affects the

likelihood that one seller's price cut would spur a matching response by the others, resulting in a mutually unprofitable price war).

Expansionary monetary or fiscal policy shifts the demand curves facing firms outwards. Since oligopolists are not typically supply- or cost-constrained, they could profitably respond by increasing output and employment, with no change in prices. That is, an elastic response is technically feasible.[4]

But unfortunately, again, it is easier and more profitable to respond by increasing prices and thus profit margins, rather than going to the trouble and expense of employing and producing more.

In my book (Chapter 6), I argue that the deterioration in economic performance over the last 20 years or so reflects a seeping away of elasticity, with oligopolists steadily becoming better at responding to increases in demand with higher prices rather than higher output and employment. This contributes to their individual short-term gain, at the long-run cost of an economy which is stuck at a mass unemployment equilibrium and is generating lower wages *and* profits than its potential. The goal of new policy initiatives must be to get the economy out of the low-level trap in which it has become entangled.

Dealing with the Problem by a Change in Regime

The situation depicted in the previous section is an example of what is technically known as a "Nash Equilibrium" — an economy in which each decision-maker is doing as well as it can, given the actions of all the other decision-makers, but the system as a whole is not necessarily performing optimally. In Canada and other developed economies in the 1980s, the main manifestation of this sub-optimal system performance is mass unemployment of labour.

The equilibrium has stubbornly resisted the pushes and pulls of orthodox macro-economic fiscal and monetary policy. What is needed, it appears, is something more radical, something that will pry the economy loose from under-employment and allow it to move permanently to a higher level of employment and output.

There are two basic directions in which we could search for this radical change within the rules of the market game: reducing costs or increasing demand.

The cost-reducing alternative has received some attention, most recently from Martin Weitzman, whose "share economy" proposal (1984, 1985) would induce employers to take on more employees by reducing up-front wage costs.

A key idea here is that while it may not look worthwhile to a group of workers in a particular industry to take a (temporary) wage cut, if *all* groups

did, the resulting fall in wage costs across the economy would induce general price cuts. This would increase real incomes, and induce multiplier effects (induced increases in demand) that could make the eventual payoff in increased employment look more attractive.

I have examined the share economy proposal elsewhere (1986), and believe that it flounders on the unreliability of the payoff in higher output and jobs. Labour unions tend to see proposed wage cuts as veiled attempts to redistribute income from workers to capitalists, at best, or simply as foolish measures, at worst, which could even increase unemployment by cutting purchasing power and altering expectations. I expect that the unions are better macro-economists in this respect than most economists.

In the other direction, there is no technical difficulty in increasing demand through conventional expansionary policies, except that as we saw the oligopolistic economy tends to pocket the proceeds from increased spending by increasing prices rather than raising output and employment.

But there is no *necessity* for this to happen. Expansion of output would not be unprofitable. On the contrary, with higher rates of capacity utilization, profit margins for most operations would improve, even with no increase in price, and total profits would certainly go up.[5] Furthermore, the eventual multiplier effects of increased output and incomes throughout the economy would eventually lead to still larger increases in profits.

The key is to somehow persuade firms not to short-circuit an economic recovery by pushing up their prices. The most direct way of achieving this is simply to *forbid* price increases, by means of a comprehensive system of price controls. With ceilings on prices, firms would have to find ways of increasing output (and productivity) as a means of improving profitability. In effect, firms would lose control over one variable — price — and would have to make the best possible use of the other instruments available to them. They would be converted from oligopolistic "price-makers" to "price-takers", simulating the behaviour of a competitive system, and delivering the superior performance that economists have always expected from competition.

Such a "regime shift" would shake the economy out of its inferior Nash Equilibrium, and set it on the path to full employment. The next section discusses how a price control policy would actually work.

The Details of Price Controls

How can we put a lid on prices without jeopardizing important objectives like efficiency and fairness? Most economists believe, almost instinctively, that this is not possible — that direct anti-inflation policies will always cause more problems than they solve, at least if they are kept in place for any length of time.

The mainstream view may be correct. However, I believe it is possible to devise a price control policy that would actually improve efficiency and

equity, as well as achieving its primary goal of preventing renewed inflation from aborting economic recovery to full employment.

The trick is to take advantage of the very feature of the modern economy — its dominance by low-elasticity, "lumpy" oligopolies — that got us into this mess to start with.

Specifically, my proposal has the following features:

1. "High-Level" Price Controls

Inflation is a general increase in retail (consumer) prices — the price of goods as they finally leave the production part of the economy and are consumed by households. With the exception noted below, only retail-level prices would be controlled.

No attempt would be made to interfere with the much larger number of prices involved in all the intermediate transactions of goods and services that take place as a commodity passes from raw material to finished product. Unless our goals are quite different (such as changing income distribution rather than achieving full employment), we are not interested in intermediate prices, including wages paid for labour services, and there would be no need to get involved with them. These prices would continue to be set as they are now — by bargaining between oligopolistic firms and unions on the basis of what the market can bear. The only difference would be that the ability of the market to bear higher costs would be constrained by a ceiling on the final price of the finished product.

It would be unnecessary to control retail prices for highly personalized products, such as haircuts or piano lessons. Such products are too highly differentiated to make price controls feasible. But a high degree of differentiation goes along with a large number of suppliers, and it is when the market consists of many small sellers (contrary to the oligopolistic norm) that competition can be relied up to keep prices from getting out of line.

In competitive industries, prices only change permanently when costs change, and most of the costs are for the sort of manufactured products that would be covered by price controls. Essentially, when the final major stage of production is a labour-intensive service activity, price controls would apply one level down. Controls are only feasible, and are only necessary, to regulate the oligopolistic price-making sectors of economic activity.

2. Direct and Implied Controls

Even in markets dominated by large firms selling standardized commodities that are amenable to control, smaller "fringe" operators often sell non-standardized "niche" products. As well, small and large firms are continually offering new and different products to consumers, in the hope of achieving a higher market share.

It would obviously be very difficult to specify the price of every fringe or new product, no matter how small its market share. And even apparently standardized commodities differ, in the eyes of consumers, in various details of quality and specification, some of which, like "taste" or "image", are impossible to quantify, much less evaluate in terms of their precise cost.

But this does not invalidate price controls. Fully comprehensive coverage would not be necessary. The key is to take advantage of the competition that always exists in markets because of the substitutability of products. So long as the prices of the major objective characteristics of the dominant products in a market were limited, competition for market share would control prices with respect to differences in minor and less tangible quality differences. The force of these competitive pressures would probably be greater than at present, because with the prices of major characteristics stable, consumers would be able to devote more attention to comparison shopping among less important characteristics, thus increasing the degree of competition — the elasticity — in markets overall.

Changes in measurable characteristics, such as size, weight, or chemical make-up, would be handled by setting "price" as a formula, calculated as a function of the various physical characteristics embodied in a product. Such formulas, which are called "hedonic price indices", can match a very high proportion of the price differences actually observed in markets, even of relatively complicated products like automobiles. Such formulas would allow sellers to vary the amount of each characteristic to suit changing tastes and technical conditions, without having to go through the fuss of clearing the "new" product's price with the price controllers.

3. Controls as an Engine of Growth

The price formulas would set ceilings on the prices charged by any firm operating in a market. But so long as price and quality constraints were satisfied, firms would be welcome to find other means of increasing profits, by selling more and/or producing more efficiently. Nor would low-cost firms be prevented from cutting prices below the ceiling, in order to increase market share. This is the "engine of growth" of competitive capitalism, and one of its main social justifications as an economic system.

If anything, price controls would speed up the engine, by focussing firms' attention on more desirable paths to higher profits.

4. Controls Must Be Permanent

This is perhaps the hardest thing for well-trained economists to accept. In the neo-classical world of perfect competition, inflation is essentially an aberration, an outgrowth of errant expectations on the part of price- and wage-setters which can, in principle, be quickly dealt with by deflating those expectations. To achieve this, a short, sharp dose of controls may be helpful (along with appropriately restrictive monetary and fiscal policy), but any extension of direct anti-inflation policy beyond, say, a year or two, would be positively

harmful (as well as unnecessary) because of the dreaded "distortionary" side-effects of controls.

But our economies are not perfectly competitive, and inflation is not an aberration. On the contrary, a tendency to inflation is inherent in a basically oligopolistic system. Thus, a permanent price policy must, perhaps unfortunately, be accepted as a necessary means of preventing inflation from continually choking off efforts to expand the economy back to full employment. A fundamental change in behaviour is required if oligopolistic firms are to stop acting as price-makers and begin acting as price-takers. Such a shift in the pricing regime could not be expected from a policy known to be temporary.

5. Accommodating Long-run Cost Changes

If controls are to be permanent, they must accommodate long-run changes in relative costs resulting from trends in technology and prices of raw materials. Even with no inflation, some commodities should go up in price, and others should fall. Prices of relatively new products tend to drop as economies of scale are realized and as efficiency lessons are learned. Mature and/or labour-intensive commodities become relatively more expensive. Prices of energy-intensive commodities, such as fertilizer, move up and down with the world price of oil. On average, in Canada, retail prices of individual commodities move up or down by around three percentage points relative to the consumer price index, each year. So even with no inflation (CPI steady), a permanently frozen price structure would result, in intolerable distortions, within a year or two, with some commodities being sold at a loss and others generating sizeable windfall profits.

However, it should not be beyond the wit of price controllers to deal with relative price changes. Precisely because they are long-term, trends that change the cost of technology can be monitored. Existing analytical tools (statistical sampling of firms' costs; a mathematical input-output model of price formation; econometric specification of price formulas) could be combined and developed into a routine procedure for managing changes in ceiling prices.

The market itself would provide much of the necessary information. In maturing industries, leading firms would show the way, as they do now, by undercutting existing prices. All the controllers would have to do is tag along behind, formalizing the new price structure as its pattern settled down. For many commodities, especially labour-intensive items which are increasingly appropriate for production in newly-industrializing countries, the prices paid for imports are a good guide to the path of market forces.

It should be emphasized that the controllers would only include truly exogenous (uncontrollable) events in their calculations of relative price changes. These might include changes in technology (that is, in the knowledge of how things are best made), and in the prices of raw materials determined by

supply and demand in world markets. They would not, in particular, allow price increases for intermediate goods (that is, semi-finished commodities) to be passed on as price increases at a later stage of production. Such prices are "endogenous" — they are determined within the system. So they should be set by the buyers and sellers themselves, subject to the crucial constraint that all intermediate transactions must be consistent with the controlled final retail price.

This proposal is the opposite of traditional wage and profit margin controls (often misnamed "price" controls), such as those administered by Canada's Anti-Inflation Board in the mid-1970s. Whereas AIB attempted to control prices by controlling costs, retail price controls would control costs by setting a ceiling on the price that could be charged for each good at the final stage of production. Such price controls would, in effect, *simulate* perfect competition by imposing the discipline of price-taking behaviour on firms. With the ultimate market price of a good taken as a given, firms (and their unions) would have to turn their attention towards reducing costs and increasing output as a means for increasing incomes.

How would the incomes of price-control wages and profits be determined within a system? In a zero-inflation economy, with no shift in the shares of labour and capital, the change in wages would be equal to the average rate of productivity growth (the rate of growth in per capita real GNP). To match the market, the price controllers should build this rate of wage change into the price formula, so that prices in areas of slower-than-average productivity growth would rise, and prices in relatively high-growth industries would fall. Such adjustments in relative prices are necessary, both to avoid windfall profit losses and gains, and to encourage activities that make the most economical use of society's resources.

This section presents a system of high-level retail price controls designed to cope with the inherently inflationary tendencies of our oligopolistic economy. No such radical-sounding proposal is likely to pass unchallenged. In the next section, I list and counter a number of fallacious arguments against price controls.

Eleven Fallacies About Controls

It is not necessary to love price controls to accept them as an anti-inflation policy. Submission to rules and laws is unpleasant when it conflitcts with personal inclinations, but so long as laws are fairly applied across society, their application can leave us all better off. So it is with the system of economic laws proposed here to deal with inflation. Permanent retail price ceilings would often be irksome for individual participants in the economy. They would be quite costly and difficult to operate. Mistakes would no doubt be made. But no policy is perfect or costless. The real point is that the benefit of beating inflation would justify a lot of inconvenience.

This section challenges a number of statements commonly made about controls. While many of these criticisms have some validity for the various wage and profit margin policies that have been attempted in the past, they are fallacious when applied to price controls as proposed in this paper.

Fallacy 1: *Price controls distort the allocation of resources by interfering with free market forces*

This is probably the most deep-seated misconception, resting as it does on the cherished neo-classical myth that the economy is really a perfectly competitive system, with prices set by invisible but super-efficient "auctioneers". In such a taut, efficient world, where prices are just sufficient to yield every firm a "normal" profit — no less and no more — intervention by heavy-handed bureaucrats would obviously mess things up.

But to repeat a point stressed throughout, if the real world were really neo-classical, neither price controls nor any other direct anti-inflation policy would be needed. The monetary squeezes of the past few years in the United Kingdom, Canada, and the United States, would have had the auctioneers slashing prices at the first sign of excess supply (unemployment). Instead, unemployment on an enormous and tragic scale has only just managed to bludgeon inflation rates down to the levels of a decade or so ago. This is because the economy is really a lumpy, oligopolistic thing, far removed from the textbook ideal of perfect competition.

This is why another policy is necessary, and why a sensible policy could work. In the real world of oligopolistic profit margins, unlike the knife-edge situation of perfect competition there is room for manoeuvre. Price controllers would have some leeway to make mistakes, just as the private sector does at present. The important thing is that long-run trends in relative costs due to technological change and changes in primary input prices would be matched by changes in relative prices, so that distortionary profits or losses do not emerge. Precisely because they are long-run trends, relative cost changes could be monitored and matched by price controllers.

What about the short run? Part of the myth about markets is that "auctioneers" are busy every day, adjusting prices up and down to compensate for temporary fluctuations in supply and demand. In fact, the use of price changes to clear markets in the short term is confined to a few perishable agricultural commodities, and to the "paper markets" for assets (stocks, bonds, foreign exchange, futures, etc.) which are not included in the consumer price index. In the great majority of consumer markets, short-term mismatches between supply and demand are accommodated by allowing stocks of inventory or orders to vary, not by costly price changes that upset customers.

Indeed, there seems to be social disapproval of "profiteering" when price increases are used to clear short-run excesses of demand over supply. In the free-enterprise United States, a great fuss is always made when auto dealers respond to a shortage of a popular new model by charging more than the

manufacturer's "recommended" retail price. What does happen is that the more negotiable dimensions of deals respond to temporary mismatches of supply and demand. Car dealers do not normally raise their own sticker prices, but they do vary the price they will pay for a trade-in. This type of activity would not be of concern to price controllers.

No such social norm discourages price *decreases*, when supply exceeds demand, and neither would the price controllers, whose concern would only be to maintain price ceilings, not floors. By keeping a careful watch on long-term trends in relative costs, and by leaving to existing market institutions the job of handling short-term fluctuations, price controllers should be able to avoid distorting the allocation of resources.

Fallacy 2: *Controls would require a huge bureaucracy*

Britain employed 77 inspectors (27 of them qualified accountants) to enforce price control legislation in 1942. The Price Commission disbanded by Mrs. Thatcher's government soon after it came to power in 1979 employed about 50 professionals out of a total staff of 600, who dealt with 8,000 "notifications" each year, many of them involving large numbers of individual price changes.

These are not huge numbers, given the size and value of the job. After all, even "market" price-setting is not costless. Bay Street and Wall Street employ thousands of professionals, most of whom are involved in price-setting, and many of whom are substantially rewarded for their labour. Retail prices are set, for the most part, by lower- to middle-level private sector bureaucrats. Under a price controls system, these jobs would be partially transfered to similar people working in a public sector bureaucracy. The work would be simplified by restriction of the market or industry level, compared to wage and profit margin control schemes that require dealings with individual firms and incur the associated compliance and/or avoidance costs.

Although the bureaucracy needed to run a permanent price controls program would not be small, there is no reason to expect it to be inflated out of proportion to the job it would be doing.

Fallacy 3: *Contols dilute quality*

It is true that for many, perhaps most, commodities, it would be impractical for price controllers to include all the relevant characteristics in their pricing formulas. Matters of taste cannot be measured objectively.

I have suggested that the prices of relevant measurable characteristics be set explicitly, and the remaining intangible factors be controlled by the market — that is, by competition for customers between sellers. If consumers were assured of value for money on most characteristics of competing products, they could then focus their attention on the remaining differences, with a consequent increase in elasticity — that is, in the responsiveness to perceived quality differentials — that would discourage sellers from diluting quality.

Since many intangible quality factors are "produced" at no cost, there would be no pay-off in cutting them back. The brand name and "image" of Coca Cola, the "flair" of Olivetti, the experience and reputation of an industry leader like IBM, the location of a corner store are all valuable assets, which it would serve no purpose to devalue.

It is in the routine parts of the production process that there is scope for cutting costs by lowering quality: by using inferior materials, or by reducing the number of quality control inspectors on the assembly line, for example. But precisely because they have become routine, these dimensions of quality could be specified in the controllers' price formulas. Even reliability can be effectively controlled by specifying the warranty offered by the seller.

Fallacy 4: *Controls lead to shortages*

Shortages can be seen as an extreme case of quality dilution. Whereas quality is reduced when sellers cut back on some of the product characteristics they offer at the going price, shortages mean a cutback in *all* characteristics — that is, in the total availability of the good.

The fear that price controls will lead to shortages seems to be a legacy of wartime conditions, under which rationing was needed to help divert about half the GNP to military uses. Such concerns are hardly relevant in times of mass national and international unemployment and under-utilization of productive capacity. Business could profitably increase production at going prices, if the demand were there. That is, there is potential in our economies to control prices and expand demand, without running into shortages.

Fallacy 5: *Controls should be temporary*

On the grounds that a little of a bad thing is better than a lot, it is often suggested that any controls program should at least be short. This would achieve a break in inflationary expectations without a build-up in costly distortionary side-effects.

This view is quite mistaken. Far from breaking down expectations, a controls program that is known to be of limited duration encourages firms and unions to "hold their breath" — to refrain temporarily from inflationary behaviour in anticipation of a great rush of price and wage increases after the controls are taken off.

The distortions that result from this behaviour offer some of the more celebrated examples of problems arising from controls. In the six-month price freeze of 1973, the U.S. consumer suffered unprecedented and alarming shortages of the great American staple, beef. This happened because farmers did not slaughter their stock, speculating that, by holding on for a few months, they would be able to cash in on higher post-controls prices. In any event, the speculators were wrong, as speculators often are. The frenzy of slaughtering that followed the lifting of controls resulted in a glut, and prices actually fell a little. But the damage was done.

Instead, controls should establish a permanent, reliable, long-term framework for non-inflationary decision-making.

Fallacy 6: *Controls should be flexible*

Flexibility is a good-sounding word, but it has been the ruin of the micro-meddling in our managed economies. Flexibility means that the outcome is up for grabs. It encourages "rent-seeking" behaviour — the employment of lawyers, accountants, and lobbyists to turn the flexible policy-maker in the desired direction. This uses up real resources (in both private and public sectors) to no productive end.

Price controls should be designed to apply widely, thus diluting the incentive of individuals to lobby against them. The scope of price controls is limited by the need to have relative prices change, but at least the program as proposed would apply at the industry level, to commodities, rather than to individual firms. As far as possible, the controllers would adjust prices up and down by the application of fixed rules, rather than through discretionary decisions.

In practice, even laws vary in interpretation and in the intensity with which they are enforced. The price control agency would be subject to lobbying, complaints, and attempts at political interference in its day-to-day business. But if, as I suggest, it is possible to specify a fairly inflexible set of rules under which controllers would operate and provided that the rules themselves are only changeable by Parliament, their resistance to interference will be higher than that of the typical regulatory agency.

Fallacy 7: *Controls never work, anyway*

Wage and profit margin controls have not had more than moderate success. But when genuine price controls were imposed during the Second World War they were remarkably successful, despite the very unfavourable economic circumstance of general shortages in consumer goods. The cost-of-living index in the United Kingdom, having increased 30 per cent from the start of the war to the end of 1941, rose only one per cent over the next four years, to December 1945, under the price controls program.

Orthodox economists, though normally not much interested in history and its lessons, are always ready to reach back through the centuries in the search for examples of unsuccessful price controls. A Roman emperor named Diocletian attempted for thirteen years to "command cheapness", with the death penalty for transgressors, and gave up. A thousand years later, Kublai Khan had a try, and also failed in due course. (No doubt these men were trying to suppress the effects of an irresponsible monetary policy, something that no serious advocate of controls would now recommend).

It is a pity that opponents of controls do not look closer to their own times for precedents. The lack of interest in the success of wartime economic management in general, and price controls in particular, is odd. The great

applied economist Lord Beveridge had no doubts, and in an almost off-hand way, as though the point were obvious, included controls in his proposal for achieving non-inflationary full employment after the war:

> Adoption by the State of a price policy is a natural and probably inevitable consequence of a full employment policy.

The full employment part was written into legislation; controls were quietly forgotten.

Total freezes in prices are credited with assisting dramatic slowdowns in inflation rates in Brazil and Israel. Although the pressing economic problem in these countries is different from that facing Canada — the need for a sharp deflation in hyper-inflationary expectations rather than the erosion of full employment through creeping inflation — their experience should be credited to the positive side of the ledger, as examples of feasible and successful direct anti-inflation policies.

Fallacy 8: *Inflation cannot be controlled internally, because world inflation rates cannot be controlled*

It is true that changes in particular world market prices cannot be adjusted away by the exchange rate. If a country exports, manufactures, and imports raw materials, such as oil, an increase in the supply price requires an increase in domestic prices relative to wages, since the country is worse off, in real terms than before. Such a deterioration in its "terms of trade" would be allowed for in price control formulas, which respond to truly exogenous price changes in raw materials.

In general, the presence of a great world market over which the domestic policy-maker has no control would be a help, not a hindrance, to domestic price controls. As a source of useful information on trends in prices, technologies, tastes, and so on, and of give competition for local sellers, the world market is an important source of price elasticity.

Fallacy 9: *You cannot control prices without controlling wages and profits*

I have suggested that if final prices were controlled directly, the cost of intermediate goods and factors of production, most notably labour, would fall into line. This would depend on the response of trade unions to price controls. If they wished, they could push wage demands up against prices, bringing about mass bankruptcies and unemployment and even the demise of the capitalist market system.

In this case, we may as well get the revolution over with as soon as possible. But it is my judgment that the objectives of western labour movements are, for better or worse, reformist at most and rather conservative in many matters. In particular, the recent econometric evidence supports the hypothesis that wage increases are aimed at no more than compensating for increases in the cost of living. Thus, if the cost of living were controlled by

retail price controls, wage controls would be redundant, and thus undesirable, given their intrinsic unpleasantness.

As well, since price controls are proposed as part of a wider policy package to enable us to reach non-inflationary full employment, the increase in employment and productivity that this would yield would allow substantial improvements in real household incomes, weakening union pressure to improve labour's position by bargaining for higher wage rates.

If it were deemed necessary to give collective bargaining a helping hand, price controls could be supplemented by a general wage order system, under which all wages would be compulsorily adjusted periodically (perhaps annually) by an amount equal to the whole economy's ability to pay. In essence, wages would follow increases (or decreases) in real per capita GNP. Such schemes have been tried before, with some success.

What about non-labour income — profits? Profits pay the return on the capital tied up in an industry, and compensate the entrepreneurs who set up and run firms for their energy and nerve. Profits also reflect luck and, on a more sinister note, the pay-off for achieving a degree of market power over one's suppliers or customers. The net result, as a number of researchers have discovered, is the existence of substantial and often persistent differences in profitability between industries, and between the firms within industries.

Until more is known about the determinants of profit differences, price controllers should probably adopt a rather cautious strategy, making an allowance in the price formula of each product for a profit rate equal to the average earned by the firms producing it over the previous few years. The important thing is that any formula should apply to the commodity, not to the individual firm producing it, so that if any firm can better the average cost performance of its competitors by improving productivity, the resulting profit gains will not be snatched away.

Fallacy 10: *Controls are "planning"*

One of the silliest ways of attacking price controls is to associate them with the failures of centralized planning. In fact, the differences are crucial. One system controls *prices*, the other *quantities*. Whereas planners in East European economies (and in the North American "military-industrial complex", for that matter) attempt to interfere with the millions of decisions made daily on what to produce, how much to produce, and where and how to distribute it, price controllers would merely set ceilings on the price at which finished commodities could eventually be sold.

The distinction is really fundamental. In a well-functioning competitive market system, the private sector is not supposed to control its own prices — they are to be set by impersonal market forces. The price controls system would, as I have stressed, simulate perfect competition by taking price-setting power away from oligopolists and investing it in the public sector.

Conclusion

This paper proposes a system of direct price controls aimed at holding the consumer price index steady while allowing individual prices to move up and down in response to long-run trends. An obvious benefit of such a policy is that it would stop inflation.

However, this is not the main purpose of controls. Current rates of inflation, though still a nuisance, are not our major economic problem. What matters most is mass unemployment, and the real mission of price controls would be to prevent the threat of inflation from side-tracking attempts to expand the economy to full employment. This would be achieved by engineering a "regime shift" from price-making to price-taking behaviour on the part of private sector decision-makers.

Although this may sound rather radical, even revolutionary, it is in fact a fundamentally conservative proposal. Very much in the spirit of Keynes, I am suggesting a means of prolonging the life of capitalism by helping to deal with one of its chronic weaknesses — the evident incapability of our economies as presently constituted to give everybody who wants it a decent job.

This weakness stems from the oligopolistic structure of mature capitalism, and my prescription follows from a particular perception of the macro-economic consequences of pervasive oligopoly. Of course, other analyses and prescriptions are possible. In particular, more fundamental reforms should be considered, such as attacking oligopolistic structures at their source, rather than just suppressing their harmful effects. I have something to say on this in my book (chapters 19-23).

The crucial point is to recognize imperfect competition as the basic characteristic of market organization. Because it has failed to reflect this reality, neo-classical macro-economics has dug itself into a big hole. By clinging to the paradigm of perfect competition, it is unable to explain unemployment except as a temporary or even illusory phenomenon, calling on an increasingly implausible bag of analytical tricks to justify this gross distortion of reality.

Economists do society and, in the long-run, themselves, a grave disservice by not facing up to the inadequacy of their doctrine in dealing with the great problems of the day. No doubt, the theoretical and practical problems of price controls are more numerous than my enthusiastic pleading has allowed. But the pay-off for a successful policy would be huge — non-inflationary full employment — and for this it is surely worth taking some risks. At the very least, the case for a direct anti-inflation policy should not be obscured by the smoke-screen of almost blind prejudice that has always seemed to choke off open-minded debate on this terribly important topic.

NOTES

1. See Tim Hazeltine, *Full Employment Without Inflation* (London: Macmillan, and New York: St. Martin's Press, 1984), pp. 35-37 for documentation. See also A. Hasan and Surendra Gera, *Job Search Behaviour, Unemployment and Wage Gains in Canadian Labour Markets* (Ottawa: Economic Council of Canada, 1982) for additional Canadian evidence.

2. For discussion and documentation of the turnaround in demographic and related factors in Canada, see S.F. Kaliski, "Why Must Unemployment Remain So High" in *Canadian Public Policy*, June, 1984; and C.M. Beach and S.F. Kaliski, "Structural Unemployment: Demographic Change or Industrial Structure" in *Canadian Public Policy*, June, 1986.

3. Set off by D.M. Lilien, "Structural Shifts and Cyclical Unemployment," in *Journal of Political Economy*, 90:4, 1982. For Canadian discussions, see M.F.Charette and B. Kaufman, *Short Run Variations in the Natural Rate of Unemployment* (Unpublished, 1985); and Lucie Samson, "A Study of the Impact of Sectoral Shifts on Aggregate Unemployment in Canada," *Canadian Journal of Economics*, August, 1985.

4. Because they have (quite sensibly) let their productive capacity shrink with the seemingly permanent decline in employment rates, firms might run into short-term supply constraints as they expand. But these could be eliminated by investments in plant and training, if the firms were confident that higher demand would be maintained. That is, the long-run average cost curve is elastic.

5. For very substantial increases in output, as stated in note 4, increased investment in plant and training would no doubt be necessary before higher profits would be realized.

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VIII

COMBATTING UNEMPLOYMENT THROUGH WORK TIME REDUCTIONS[1]

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The dramatic rise in the Canadian unemployment rate over the early 1980s has resulted in a renewed search for alternative policies. This paper assesses the feasibility of three types of policies that involve reductions in work time: legislated or negotiated reductions in the standard work week; encouragement of voluntary work time reductions with proportionate reductions in pay through job sharing, longer vacations, sabbatical leave and early retirement; and Short-Time Compensation (STC) policies in which layoffs are avoided by using unemployment insurance benefits to partially compensate workers for temporary reductions in the work week. For convenience, this group of policies based on work time reductions will be referred to as employment sharing.

A striking feature of Canadian labour markets is the extent to which rather modest fluctuations in the demand for total labour hours cause dramatic changes in the unemployment rate. It is instructive to recall the experience of the 1982 recession. As Table 1 indicates, total hours worked per week dropped by 3.8 per cent between 1981 and 1982. This reduction in total hours of work was accomplished mainly through a reduction of employment rather than a reduction of average weekly work hours. Employment dropped 3.3

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Table 1

Changes in Hours and Employment during the 1982 Canadian Recession

	1981	1982	Absolute Change	% Change	Change as % of 1981 Labour Force
Total hours worked per week (thousands)	381,247	366,600	-14.647	-3.8	—
Average hours worked per week	34.6	34.4	-0.2	-0.6	—
Employment (thousands)	11,006	10,644	-362	-3.3	-3.0
Labour force (thousands)	11,904	11,958	+54	+0.5	+0.5
Unemployment (thousands)	898	1,314	+416	+46.3	+3.5
Unemployment rate (per cent)	7.5	11.0	+3.5	+46.7	—

Note: Average hours per week includes full-time employees, part-time employees and employees not at their job in the reference week due to factors such as vacation, illness or labour dispute.

Source: Statistics Canada. 1984: Table 1 and 27, and calculations by the author.

per cent during 1982, while average hours worked dropped by only 0.2 hours per week, a 0.6 per cent reduction. The 3.3 per cent reduction in employment represented a loss of 362,000 jobs and comprised the bulk of the 416,000 increase in measured unemployment between 1981 and 1982. The net result of this process was a sharp rise in the unemployment rate from 7.5 to 11.0 per cent, an increase of almost 50 per cent.

If average hours in 1982 had been reduced by 1.5 hours per week from the 1981 level, employment would have remained above 11 million (given total hours of work in 1982) and the 1982 unemployment rate would have remained at 7.5 per cent instead of rising to 11.0 per cent.[2] If the economy had adapted to the recession through fluctuations in hours rather than employment, relatively small changes in the average work week (about one hour per week) could have eliminated a rather severe rise in the unemployment rate of 3.5 percentage points.

The first section of this paper provides a theoretical framework for employment sharing policies in a competitive market economy. Subsequent sections

deal with several specific policies, while the final section summarizes the policy implications of the analysis.

The Economic Rationale for Employment Sharing

A gradual reduction in hours of work has been observed in Canada over the century or more for which data are available. In manufacturing, the sector for which the data are most complete, the standard work week was reduced from 64 hours in 1970 to just under 40 hours in 1982 (Ostry and Zaidi, 1979; Aw, 1982 and calculations by the author). In the post-war period, the reduction in weekly hours was accompanied by increases in annual vacation days and holidays. The long-run reduction in work time mainly reflects increases in the real wage rate. As workers have become more productive they have chosen to take part of the increase in the form of higher real annual incomes, and part in the form of decreased annual work time. If productivity continues to rise in the future, these long-term trends are likely to continue, and workers' quality of life will be enhanced by further reductions in work time.

However, the employment sharing policies considered in this paper are not simply a component of the long-run reduction in work time. They are a means of redistributing work during periods when short- or medium-term factors have raised the unemployment rate beyond its "normal" level.

There is no doubt that it would be better to eliminate such deficient-demand unemployment through economic recovery, rather than attacking its effects through employment sharing. But if economic or political constraints such as concern about the deficit or the inflation rate prevent deficient-demand unemployment from being eliminated, policies to share employment are more equitable and efficient than policies that generate layoffs and unemployment.

Standard economic analysis often concludes that, under specified conditions, competitive markets will lead to an outcome that is "efficient", in the sense that no rearrangement could make one person better off without making someone else worse off. This conclusion presumes, however, that the effects of any transactions are confined to the two parties involved. If there are third-party effects or externalities, competitive markets will not lead to an efficient outcome and intervention or regulation is required to achieve efficiency. A classic example is the case of a firm which, through air pollution, harms or inconveniences third parties who have no practical method of expressing their concerns through a market mechanism.

In the case of employment sharing, an externality exists because a reduction in employment may impose costs on taxpayers in the form of increased expenditures on unemployment insurance and welfare. In addition, recent Canadian evidence indicates that the stress of layoffs or the prospect of layoffs may induce emotional and health problems which result in increased public expenditures on health services (Canadan Mental Health Association, 1984; Kirsh, 1983; MacLaren et al., 1983). The employer and current employees have no economic incentive to take account of such third-party

effects when contemplating the use of employment sharing. As a result, the market system can be expected to result in an inefficiently low use of employment sharing in response to fluctuations in the demand for labour.

Employment sharing is also more equitable as a response to reductions in demand for labour. The small minority of individuals who become unemployed as a result of a drop in overall demand for labour bear a disproportionate share of the burden of recession. When one considers that the recession is induced or at least tolerated by government to achieve a goal that benefits society as a whole (a reduction of inflation), the inequity of relying on employment reductions as the mechanism of adjustment is clear.

Reducing the Standard Work Week

Some participants in the economy, particularly the labour movement, have proposed that unemployment be relieved by reducing the standard work week significantly, say to 35 hours per week, with no drop in weekly income. This could be accomplished through collective bargaining or through amendments to employment standards legislation. A complementary policy would be an increase in the overtime premium from time-and-a-half to double time, to discourage employers from increasing overtime in response to a reduction in standard hours.

The suggestion that hours be reduced without cutting income is somewhat deceptive. A reduction in weekly hours from 40 to 35 with no change in weekly income is equivalent to an hourly wage increase of 14 per cent (40/35 = 1.14). Although nominal weekly income would be maintained, the employer's ability and inclination to negotiate present and future increases in the hourly wage would be reduced correspondingly. In effect, the reduction in weekly hours is being traded against potential increases in weekly income that the employees might otherwise have negotiated.

There are four factors which should be considered in assessing the desirability of reductions in the standard work week as a means of combatting unemployment: enforceability, reversibility, induced productivity effects, and the impact on labour costs and employment.

Although several Canadian jurisdictions (federal, British Columbia, Manitoba, Saskatchewan and Yukon) currently specify a 40-hour standard work week, most (Ontario, Quebec, Alberta, the four Atlantic provinces and Northwest Territories) specify a standard work week of 44 hours or more (Labour Canada, 1982). Current labour standards legislation thus appears to be superfluous for most employment situations, because a standard work week less than (or equal to) the legislated maximum has been set by personnel policies or collective bargaining. If a significant lowering of the legislated standard caused the legislation to become binding in a substantially larger number of employment situations, it is likely that considerably more resources would need to be devoted to enforcement of the legislation. In addition, in some cases, both the union and management would prefer a work week greater

than the legislated standard. It is notoriously difficult to police a system in which the government attempts to prevent a mutually agreeable transaction between two parties.

Enforceability is not a problem if the reduction in the standard work week is achieved through collective bargaining, since one or both of the parties has an interest in enforcing the agreement. The potential scope of collective bargaining is, however, considerably more limited than employment standards legislation. With a decentralized bargaining system such as Canada's, it is unlikely that widespread reductions in the standard work week could be achieved in the immediate future through the collective bargaining process.

The second potential problem with the use of reductions in the standard work week to combat deficient-demand unemployment is that it may be difficult to reverse the process if the economy recovers and deficient-demand unemployment is eliminated. In the past, reversals have generally not occurred, since employment standards legislation and the collective bargaining process have been used to achieve permanent reductions in the standard work week as part of the long-term trend of work time reductions outlined in the previous section. If the government were to temporarily reduce the standard work week to combat deficient-demand unemployment, the temporary nature of the change should be made explicit through the use of a "sunset" clause restoring the standard work week to its previous level after a maximum period of, say, one or two years. Renewal of the legislation would be contingent upon the degree of deficient-demand unemployment at the time of expiration.

European experience with legislated reductions in standard hours to combat unemployment reveals a third complication — an induced increase in productivity. When France, for example, reduced the standard work week from 40 hours to 39 hours, most firms were able to adapt with very little change in work organization: "Nearly one reduction in two took the form of earlier closing on Friday evenings. Nearly one in four was achieved as a result of a twelve-minute reduction at the end of each day" (Barou, 1984:10). Government estimates suggest that the 2.5 per cent reduction in average hours increased employment by only 0.5 per cent. Similar results were observed for half-hour to one-hour work week reductions in Belgium in 1983 (Barou, 1984:12). And Gorres' (1981:15) review of a number of European studies shows that 30 to 70 per cent of a work week reduction is consistently offset by an induced rise in productivity, suggesting that a "cautious" approach of reducing the standard work week to 39 hours will have minimal impact.

Some evidence indicates there is enough "slack" in the work pattern of many organizations that minor reductions in hours can be accommodated without the need to alter the level of employment. One Canadian study (Half, 1984) suggests that the typical employee engages in "time theft" of three hours and 42 minutes per week. It is likely, however, that more substantial reductions in hours could not be accommodated by productivity increases, and would

result in a larger proportion of the reduction in hours being translated into increased employment. But if the policy is to be at all effective, a substantive reduction to, say, 35 hours per week would be required.

It is perhaps somewhat misleading to call such a substitution of leisure time on the job for leisure time off the job a productivity increase. Since the parties had the option of rearranging the work schedule in this fashion without a legislated change in the standard work week, and chose not to do so, one could argue that the parties must be worse off as a result of this induced productivity increase.

The final factor to be considered in assessing the impact of a reduction of the standard work week is the effect on labour costs and total hours of employment. A reduction in average hours may increase unit labour costs as a result of an increase in employee-specific employment costs such as health insurance premiums. Unit labour costs may be also be driven up by an increase in hours paid at overtime rates, if the firm is unable to completely eliminate the use of overtime because of unanticipated production or sales fluctuations. The rise in unit labour costs will result in a reduction in the total hours of labour demanded, assuming the usual downward-sloping demand curve for labour. A review of the empirical evidence (Hamermesh, 1976) suggests that, on average, hours of employment drop about 0.3 per cent for each per cent rise in wage costs. Such reductions would partially offset any employment gains from reductions in average hours.

Voluntary Work Time Reductions

An anomalous feature of the labour market is that, at the same time that a small but significant percentage of the labour force is involuntarily unemployed, a significant percentage of the labour force is working more hours than desired. One category of employment sharing policies comprises attempts to increase employment by encouraging reductions of work time, with proportionate income reductions, by individuals who desire such reductions.

A 1978 survey conducted for the U.S. Department of Labor attempted to determine how far the typical American worker was willing to reduce his or her work time in exchange for a proportionate reduction in income. The sample of 954 persons, designed to be representative of the U.S. labour force, was asked the maximum percentage of their current yearly income that they would be willing to give up in exchange for reduced work time under each of five employment sharing options.[3].

Table 2 presents the results for reductions in the work week and the work day. As expected, a clear majority (about three-quarters of the sample) indicated satisfaction with the current length of the work week by responding that their preferred option was no change. Of the respondents who indicated a preference for some reduction in the work week, 4.5 per cent of full-time employees indicated that they would be willing to give up 20 per cent of their income to have one day off per week, implying a reduction of 0.9 per

Table 2

Employee Preferences for Reductions in the Work Week and the Work Day

Employment Sharing Option	Per Cent of Full-Time Employees Selecting Option	Reductions as Per Cent of Total Work Time
Work Week reduction		
(a) no change	73.8	0
(b) 2% for 50 minutes off, 1 work day each week	11.6	0.232
(c) 10% for 4 hours off, 1 work day each week	7.6	0.760
(d) 20% for 1 full work day off each week	4.5	0.900
(e) 40% for 2 full work days off each week	0.9	0.360
(f) 50% for 2.5 full work days off each week	1.6	0.800
Total	**100.0**	**3.052**
Work Day Reduction		
(a) no change	77.0	0
(b) 2% of income for 10 minutes off each day	8.7	0.008
(c) 5% of income for 25 minutes off each day	5.8	0.290
(d) 12% of income for 1 hour off each day	5.5	0.660
(e) 30% of income for 2 hours off each day	1.6	0.480
(f) 50% of income for 4 hours off each day	1.5	0.750
Total	**100.0**	**2.188**

Source: Best. 1982: 38-39, and tabulations by the author.

cent in total work time (.20 times 4.5%). Similarly, 1.6 per cent of full-time employees would be willing to work 2.5 days per week with a 50 per cent reduction in income, implying a 0.8 per cent reduction in total work time.

Overall, 26.2 per cent of full-time employees would prefer a shorter work week, with a total reduction in work time of 3.1 per cent. The data also indicates that 23 per cent of employees would prefer a shorter work day, with a total reduction in work time of 2.2 per cent.

Employee preferences for various degrees of increased vacation, sabbatical leave, and earlier retirement are given in Table 3. The data indicate that 42.2 per cent of employees would be willing to give up some percentage of their annual income to obtain a proportionate decrease in work time in the form of increased annual vacation. The implied reduction in total work time is 2.6 per cent.

Somewhat surprisingly, given its rareness in the work force, 42.6 per cent of full-time employees also indicated they would be willing to give up some

Table 3

Employee Preferences for Reduction in Work Year and Work Life

Employment Sharing Option	% of Full-Time Employees Selecting Option	Reductions as % of Total Work Time
Increased Annual Vacation		
(a) no change	57.8	0
(b) 2% of income for 5 extra days' paid vacation	23.2	0.464
(c) 5% of income for 12.5 extra days' paid vacation	8.5	0.425
(d) 10% of income for 25 extra days' paid vacation	6.2	0.620
(e) 20% of income for 50 extra days' paid vacation	2.2	0.440
(f) 33% of income for 87.5 extra days' paid vacation	2.0	0.660
Total	**100.0**	**2.609**
Introduction of Sabbatical Leave		
(a) no change	57.4	0
(b) 2% of income for 7 weeks' paid leave after 6 years' work	24.4	0.008
(c) 5% of income for 17.5 weeks' paid leave after 6 years' work	8.0	0.290
(d) 10% of income for 35 weeks' paid leave after 6 years' work	4.8	0.660
(e) 15% of income for 52 weeks' paid leave after 6 years' work	4.8	
Total	**100.0**	**2.088**
Early retirement		
(a) no change	64.0	0
(b) 2% of income for 5 days' early retirement per year worked	17.6	0.488
(c) 5% of income for 12.5 days' early retirement per year worked	8.1	0.400
(d) 10% of income for 25 days' early retirement per year worked	5.9	0.480
(e) 20% of income for 50 days' early retirement per year worked	4.4	0.720
Total	**100.0**	**2.227**

Source: Best. 1981: 38-39, and tabulations by the author.

proportion of their annual income for an extended paid leave after six years' work. Almost five per cent, for example, would be willing to give up 15 per cent of their annual income for a full year of paid leave every seven years. The total potential work time reduction through increased sabbatical leave is 2.1 per cent.

Earlier retirement was of interest to 36 per cent of the employees in the sample, for a total reduction in work time of 2.2 per cent. The most popular option was a two per cent reduction in annual income to obtain five days' earlier retirement for each year worked.

It would be incorrect to simply add up the preferences for work time reduction for the five employment sharing options, because of the danger of double counting. Employees, for example, might have expressed a desire to shorten both the work week and the work day when the options were presented separately, but may not wish to do both simultaneously. Counting only the employment sharing option for each employee with the greatest proportionate reduction in work time, the data indicate that 59.3 per cent of respondents desire employment sharing corresponding to a 4.7 per cent reduction in total work time.

A 4.7 per cent reduction in work time may translate into a smaller increase in employment, due to the induced productivity effect and the impact of increased labour costs on total hours demanded. On the basis of some European evidence (Social and Labour Bulletin, 1984) an employment replacement rate of 0.2 is assumed for small reductions in work time (five per cent or less), and a replacement rate of 0.5 is assumed for larger reductions (10 per cent or more). The implication is that a work time reduction of 4.7 per cent would produce a 2.0 per cent rise in employment. A change of this magnitude is obviously not a panacea for the unemployment problem, but is significant relative to the 3.3 per cent drop in employment that took place during the 1982 recession.

It is important to ask why employees who desire reduced hours do not rearrange their work schedules to achieve the desired end. A full-time employee could switch to part-time work, or arrange a sabbatical by quitting or taking an unpaid leave of absence every seventh year (financed by saving 15 per cent of his or her salary for six years). Such arrangements may be inhibited if the employee would suffer a financial penalty, such as a lower wage and reduced fringe benefits for part-time work, or loss of job, lost seniority or reduced chance of a promotion following a self-financed sabbatical. The financial penalties presumably reflect costs to the employer, although there is also evidence of discrimination with regard to part-time work (Wallace, 1983:21).

But while the financial penalties may accurately reflect costs to the individual employer and be sensible from the employer's viewpoint, they may be inefficient and harmful to society because of the externality involved. It quickly becomes clear that the employer has no incentive to take account of

the savings which employment sharing creates for society through reduced expenditures on unemployment insurance, welfare and health programs. A conventional unemployment insurance system designed for employees out of work for the full week results in a serious bias against temporary reductions in work hours, and towards the use of layoffs.[4] Short-Time Compensation (STC) eliminates this bias by allowing workers to draw UI benefits on a temporary basis to partially compensate for reduced weekly hours of work.

As an example, a firm could avoid laying off 40 per cent of its workforce by adopting a three-day work week, with employees receiving UI benefits on the two days per week they are not at work. A STC program simply redistributes the UI benefits that would otherwise have been paid to the laid-off workers. Instead of two employees receiving UI benefits five days per week, five employees receive benefits two days per week. A STC program has been in effect in Canada since January, 1982. Since the advantages and disadvantages of a STC program have already been assessed by the author (Reid, 1982), only a very brief summary of the main points will be given here.

In the example outlined above, an employee on a STC program would receive wages equal to 60 per cent of his or her normal weekly income for the three days worked and UI benefits equal to 24 per cent (.60 times 40%) of his or her normal weekly income for the remainder. This yields a total income equal to 84 per cent of normal weekly earnings and the employee receives two extra days of leisure per week. Such a scheme obviously benefits those employees who would have been laid off, since they avoid the more substantial drop in income and the psychological effects of a layoff. Somewhat surprisingly, however, the empirical evidence and economic theory suggest that the provision of subsidized leisure time through a STC program will also benefit those employees who were not threatened with layoffs. Studies have shown that the response of employees participating in the Canadian STC program is overwhelmingly favourable (Employment and Immigration Canada, 1983).

Firms may also benefit from a STC program, because small increases in fringe benefit costs are outweighed by avoiding the cost of layoff and recall, and of hiring and training replacements for any laid-off employees who do not respond to recall when the firm returns to full production.

From the government's viewpoint, UI expenditures under the Canadian STC program were about 1.35 times the estimated cost of a conventional UI system. This cost increase resulted mainly from two unusual program design features which are not inherent in the STC concept. The cost increase could be eliminated or substantially mitigated by reducing the UI benefit rate slightly (say, to .50) to compensate for the lack of a two-week waiting period under the STC program, and an individual's UI benefits under the STC program could be deducted from his or her entitlement to conventional benefits if he or she is laid off at the expiry of the STC program.

In assessing the cost impact of STC, it is also important to note the indirect savings to government from a reduction in stress-related health problems. Finally, and most importantly, STC is more equitable than layoffs and conventional UI.

Policies to Promote Employment Sharing

In assessing the desirability of various policies for society, it is important to consider both the benefits and the costs of each policy. It is equally important, especially for employment sharing policies, to consider the equity of each policy — a process that necessarily involves value judgements. In periods of deficient demand for labour, efficiency arguments arising from the third-party effects of layoffs suggest government should adopt activist policies to encourage employment sharing. In the author's view, equity is also increased by employment sharing since it involves a more equal sharing of the burden of a recession. The policy recommendations contained in this concluding section reflect these principles.

One innovative and attractive option for combatting unemployment is to amend employment standards legislation to give employees the right to engage in voluntary employment sharing during periods of deficient-demand unemployment. For example, in addition to the minimum two weeks' paid vacation now specified in most employment standards legislation, employees could be given the right to take up to one month of unpaid annual leave without loss of seniority. Similarly, the right to a sabbatical leave could be provided every fifth year, by spreading four years' salary over five years, a practice pioneered by teachers in their "four over five" plans. Employment standards legislation specifying a maximum number of work hours per week could also be modified to enable each employee to engage in job sharing, by reducing his or her work week as low as 20 hours per week with a proportionate reduction in pay. Although such policies may involve costs and inconvenience, simulations by Meltz et al. (1981) suggest the impact is fairly modest. Such cost increases would be minor compared to the savings to society from reduced expenditures on social programs and the reduction of inequities in the labour market.

A policy amending employment standards legislation to impose a temporary reduction in the standard work week has great potential for reducing unemployment because of its wide application, but also some significant drawbacks. A "sunset" clause limiting the duration of the reduction would be necessary, to emphasize the temporary nature of the policy and ensure its reversibility. Since European evidence has indicated that a small change (say one hour per week) would be mainly offset by an induced productivity effect, a bold policy imposing a substantial reduction (four or five hours per week) would be required to have a significant impact on employment. The policy would also require a significant increase in the resources devoted to enforcement of the policy. Despite these potential costs, however, the policy is worth trying because its potential employment benefits are so great. Actual

experience with the policy would then permit a more rigourous assessment of its cost and benefits.

Reductions in the work week negotiated through the collective bargaining process are not subject to enforceability problems. But the potential impact will be narrower than changes in employment standards legislation, due to the decentralized nature of the Canadian collective bargaining system and because much of the labour force is not covered by a collective agreement. Unions are also likely to regard negotiated reductions in work time as permanent contract improvements rather than temporary changes to combat deficient-demand unemployment. Thus, while negotiated reductions in work time may be desirable, they cannot be relied upon to have a significant impact on the unemployment problem.

The government should maintain and strengthen its existing work sharing program, in which unemployment insurance funds are paid as short-time compensation to workers whose hours are temporarily reduced to avoid layoffs. The STC program is required to prevent the unemployment insurance system from creating a serious bias in favour of layoffs and against temporary reductions in hours as a response to a reduction in demand for labour. Benefit-cost analysis (Employment & Immigration Canada, 1983) suggests the measurable benefits of STC exceed costs to society by a ratio of about 1:4. Including some of the effects which are more difficult to measure, such as the reduction in the social costs of unemployment, would raise the benefit-cost ratio substantially (Reid and Meltz, 1984).

The current STC program could be strengthened by extending the maximum benefit period to that of conventional UI benefits, currently 50 weeks. Administration of the program could also be streamlined by recognizing STC as an establishment-based program, rather than an individual-based program. If information on work hours and distribution of STC benefits were handled at the establishment level, as it is in the California STC program, administrative procedures would be much more efficient than the current individual-based STC system.

Finally, a number of institutional features of Canadian labour markets represent unintended barriers to optimal employment patterns. Since these barriers create inefficiencies, there is a strong argument for eliminating them even if the economy is not experiencing deficient-demand unemployment. First, the ceilings on employer and employee payroll taxes should be specified in hourly rather than weekly (or annual) terms, to prevent a cost increase when hours are reduced by employment sharing. Similarly, privately negotiated fringe benefits and benefits provided through employment standards legislation should be pro-rated according to hours worked, to ensure that they do not become an unintended barrier to employment sharing for either employees or employers. Third, labour relations boards should place part-time and full-time workers in the same bargaining unit, to minimize

differences in contract provisions which could affect the willingness of employees to engage in employment sharing.

One of the virtues of the range of employment sharing policies advocated in this paper is that they represent a realistic set of options for combatting unemployment without a significant increase in government expenditure — a considerable advantage when a major concern of government is the size of its deficit. Although employment sharing is clearly not a panacea for unemployment, it has the potential to make a small but significant contribution to the resolution of this most important problem.

NOTES

1. Some of the issues raised in this paper are explored by the author in more detail in a 1985 background study for the Royal Commission on the Economic Union. An earlier version of this paper was presented at the conference, Unemployment: Can it be Reduced? An International Perspective, University of Toronto, November 28-30, 1984. The author is grateful for helpful discussion of these issues with Harvey Brenner, Sam Ginden, Morley Gunderson and Craig Riddell, and for useful comments from two anonymous referees.

2. A 7.5 per cent unemployment rate applied to the 1982 labour force implies employment of (1-.075) 11,958 = 11,061 thousand. This results in average weekly hours of 366,600/11,061 = 33.1, a reduction of 1.5 hours per week from the 1981 average. These calculations ignore any induced changes in participation rates, productivity, or unit labour costs.

3. Similar broad interest in work time reductions in Canada is indicated by the preliminary results of a Conference Board of Canada survey appended to the June 1985 Labour Force Survey.

4. Under conventional UI, any earnings in excess of 25 per cent of weekly benefits are deducted from benefits, effectively excluding from the program anyone continuing to work two or more days per week.

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IX

SHOULD WAGE SUBSIDIES BE USED TO FIGHT UNEMPLOYMENT?

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The function of a wage subsidy is to improve the terms under which employers can hire labour. In its most standard form, it involves a direct grant or a reduction in tax liabilities, though it can take on various other forms. Its operation as a job creation tool is straightforward. One thinks of the potential jobs which are at the margin, activities which firms can undertake but which so far have been rejected because they are just below the required level of profitability. Being able to hire labour at a net wage somewhat below the current market rate will reduce the cost of some activities and make them profitable.

There are attractions and problems associated with this strategy. But in general, wage subsidies should not be seen as a panacea, or even as the major thrust of a policy to reduce unemployment. They will work best if they are part of a coordinated package of policies, but they are not a substitute for the management of aggregate demand — in fact, they are unlikely to be effective if they are not harmonized with appropriate monetary and fiscal policy. At the same time, some of the advantages of wage subsidies make them an appropriate policy at the present time.

Wage Subsidies and the Macdonald Commission

Having developed this argument in a background paper for the National Economic Summit last March, we were pleased to see that limited use of wage subsidies as part of a larger package was recommended in the Report of the Macdonald Commission. In conjunction with reforms to the Unemployment Insurance system intended to mitigate systemic barriers to labour market adjustment, the Commission calls for the establishment of a Transitional Adjustment Assistance Program (TAAP), to reduce "structural and frictional unemployment by helping Canadians to adjust to new labour market opportunities." It includes more funding of on-the-job training, subsidies for early retirement, mobility grants to unemployed workers who can find a job at a new location, and portable wage subsidy programs. To benefit from TAAP, an unemployed worker would have to satisfy a set of eligibility requirements.

The wage subsidy component is described only briefly. "Since TAAP beneficiaries might often have been without jobs for some time, and since most would probably belong to older wage groups, they might often be at a competitive disadvantage in seeking employment. This disadvantage could be largely or entirely overcome by providing them with a portable wage subsidy." A "portable" wage subsidy is one tied to a worker, presumably negotiable with any employer. However, wage subsidies need not be attached to particular workers in the way the Commission envisions them; they may be made available to business on a general basis or within specific industrial categories. Further insight into the Commission's thinking on an integrated job program is found in a paper by Jonathon R. Kesselman, in the first volume of background studies prepared for the Commission.[1]

The Commission's broader proposal regarding the unemployment insurance system and the above-mentioned policy initiatives is consistent with our view of wage subsidies. The Commission sees the need to reduce the long-term or equilibrium unemployment potential in the Canadian economy. It believes that the non-accelerating inflation rate of unemployment (NAIRU) is as high as 6.5 to eight per cent. Since there is a strong belief on the part of policymakers, which is surely supported by a general political consensus, that acceleration of the inflation rate should be avoided, this range of 6.5 to eight per cent is the best unemployment level we can hope for at present, and will be looked upon as full employment.

Compared to an unemployment rate of nearly 10 per cent, such an objective represent a great step forward. From the point of view of economic efficiency and social welfare, however, it is still dismal. Reducing the NAIRU is a matter of changing the structure of the labour market. While it is not the most important step in such change, the introduction of a well designed wage subsidy would help the labour market adjust to excess supply more easily, in part because it can target some of the workers who remain unemployed when the NAIRU is reached.

Pros and Cons

Let us now turn to a brief account of the attractions and problems involved in coming up with a "well designed subsidy". The following factors make wage subsidies an appealing form of employment policy:

- They are direct and visible. This makes them politically attractive, because the public can see that something is being done. This perception may also contribute to business and consumer confidence, thus contributing to the buying momentum which is ultimately necessary for an economic recovery.
- They can be targetted to particular categories of workers, industries, or regions.
- Wage subsidies can offset distortions in labour markets created by other government policies. It is argued that from the employer's point of view, wage levels are too high for some of the jobs which young and unskilled workers can do. Various government policies (such as the minimum wage, unemployment insurance benefits and high marginal tax rates), which help to support these wage levels, may be difficult to remove because they are fulfilling other objectives. An alternative is to offset their effect by providing a wage subsidy.
- In the present political environment, in which broadly based expansionary fiscal and monetary policies and growth in the public sector are anathema to government, wage subsidies become more attractive. Even if equal or greater job-creating potential can be found in other policies, the fact that wage incentives are directed toward job creation in the private sector makes them more politically acceptable. Furthermore, critics of Keynesian policy fear that increases in direct government services are very difficult to terminate, while wage subsidies can more easily be temporary.

The difficulties encountered in designing and implementing an effective wage subsidy include the following:

- A wage subsidy will not work if there is insufficient demand for the goods produced by newly employed workers. If employers perceive this ahead of time, they will simply not participate in the program. If they do not accurately perceive this problem where it exists, they will find participation a losing proposition and are not likely to continue with it.
- Wage subsidies are really a matter of harmonizing macro-economic and micro-economic policy. If a wage subsidy is introduced and nothing else has changed, the program creates additional income and spending, both directly because the subsidy is paid out, and indirectly because of multiplier effects and possible effects on investment and exports. But while there is no general reason to doubt that these demand increases are sufficient to take up the aggregate output of the extra workers, their actual

ability to do so depends on a wide range of assumptions and cannot be taken for granted. The problem has been studied with the use of simulation models.[2] While the results are not conclusive they do not promote confidence in wage subsidies, with some of the authors arguing that aggregate demand management is a more effective way to deal with unemployment.

- Fully effective targetting of *new* jobs is impossible. It is impossible to implement a genuinely "marginal" wage subsidy, to know whether an employer who applies for a subsidy and claims that a new job has been created would not have had the same work done without the subsidy. This factor increases the cost of the program, not only because subsidies will be paid for jobs that are not truly new, but because of the cost of administrative attempts to reduce the number of undeserving applicants who are paid. The latter cost may be borne both by the government and by legitimate beneficiaries whose activities have to be inspected more extensively.

- As a partial solution to this problem, it has been suggested that an arbitrary benchmark be used to define new jobs. Firms applying for a job subsidy would have to report the number of people employed in their firm on a given date (for instance, on the day the policy was announced). The firm would then be eligible for a subsidy for any jobs beyond the benchmark number, during the period of the policy. Some of the new jobs would have been created anyway. But it is assumed that it is better to pay the subsidy in these cases than to set up a complex administrative apparatus in an attempt to enforce true compliance. Such procedures will not work, will be costly, and will discourage some deserving applicants.

- This benchmark system differs from the approach adapted by the Macdonald Commission, where the subsidy is tied to the worker. The Commission does not indicate how it would ensure that the subsidized worker is not simply taking a job that would have gone to someone else.

- A "benchmark" marginal subsidy supports growing firms and discriminates against declining firms. It may also discriminate in other ways. If, for instance, the subsidy is provided in the form of a reduction in tax liabilities, firms with insufficient taxable income and a lower marginal tax rate benefit less than other firms.

- A given wage subsidy may appear to be creating new jobs but may simply be replacing jobs lost at another firm. The firm receiving the subsidy can, other things being equal, produce goods at a lower cost than its competitor. The competitor's sales fall and workers are laid off. This "replacement effect" results from competition between firms that is normally viewed as healthy, but which may be questioned in a context where a wage subsidy supports one firm at the expense of another. There is no

obvious, practical way of detecting and offsetting the replacement effect, beyond making the wage subsidy equally available to all firms.

- The separation of operational and financial functions in large firms may mean that some employers do not take advantage of wage subsidies, because management personnel responsible for new jobs are not concerned with, or made aware of, the financial advantages of a particular incentive program for which the firm is eligible.
- The gains from wage subsidy programs may be ephemeral. In the case of summer jobs for students or winter works projects, this may be intentional. In other cases, however, there is likely to be a desire to create permanent jobs.
- One can assume in general that a worker hired due to a job subsidy does not have a marginal product equal to his or her unsubsidized wage. If such a worker is to remain employed after the subsidy is removed, some change must take place during the program period. For instance, the worker's productivity might increase through a process of learning by doing, or an infant firm might come of age. However, unless the recipients of subsidies are carefully chosen and the program is in place for a considerable time, there is no assurance that a subsidized job will end up a permanent job.
- For various reasons, if wage subsidies were subject to careful cost-benefit calculations, it is likely that the net economic benefit of most programs would be considerably less than the value of the income generated by the extra jobs created. For instance, an unemployed person who finds a job due to the wage subsidy will normally have had some probability of eventually finding work, without the subsidy. Consequently, it is wrong to assume that his or her output is a permanent net gain to the economy. While this question cannot be fully explored here, it clearly ought to influence any evaluation of job incentive programs.[3]
- A survey in the U.S. suggests that an American wage subsidy program "was much less cost-effective than its proponents had forecast because they seriously overestimated its ability to create jobs".[4] This one study is not conclusive, but suggests the need for a similar study of Canadian firms involved in job incentive programs.

Some of the problems we have noted are obviously more threatening to the effectiveness of wage subsidies than others. The most difficult questions in terms of whether a program will effectively reduce unemployment are the demand for the additional production involved and the firms' resistance to using the subsidies. No one, however, has argued that reducing unemployment in Canada will be easy. On balance, we think wage subsidies have a role to play.

Paying the Cost

The question of how much a wage subsidy program will cost is too complex to be dealt with in depth in this article. It obviously depends on how extensive the coverage is to be, but the important aspect of the question is the *net* effect per dollar of subsidy on the initiating government's budgetary deficit. An answer would require a series of simulation exercises on a full-scale econometric model. But it is safe to say that the net cost of a wage subsidy program will be less than the direct payments of subsidies. Some of the direct expenditures will be recaptured due to the increase in economic activity brought about by the program.

An implication of this recapture of tax revenue is that the tax increase required to run a "budget-neutral" program will be less than the amount of subsidies paid. Of course, trying to run such a budget-neutral program has its special pitfalls, since any tax increase will reduce aggregate demand and tend to counteract the operation of the wage subsidy. A net positive effect on aggregate demand is still possible, however, because the tax increase could apply to higher-income earners, while the proceeds would obviously be received at the low end of the income scale. Some of the increase in tax revenue will thus come out of savings and, since low wage earners are likely to spend all of their increased disposable income, there will still be some increase in demand to take up the goods produced.

Using the tax system to divert savings into consumer expenditure draws attention to another reason that a wage subsidy is of interest in Canada. Unlike the U.S. experience, Canada's high unemployment is clearly related to "oversaving". In late 1985, the national personal savings rate rose to 13 per cent of disposable income, compared to a rate of less than two per cent in the U.S.

However, to be realistic, the net effect on aggregate demand of a wage subsidy program, financed by a tax increase in the middle-to-upper income bracket, would be small. For a wage subsidy program to have a more substantial impact, either a short-term, planned increase in the deficit or some other financing method would be necessary.

A path to an alternative financing scheme can be found by looking upon the wage subsidy as part of a larger program. For example, the Macdonald Commission's overall program for reforming the unemployment insurance system and enhancing the process of labour market adjustment is designed to be budget neutral. Savings would be generated by tightening up benefit payments, and switching funds over to support disadvantaged workers through the TAAP. At the maximum level of insurable earnings, the recipient of unemployment compensation receives $6.60 per hour of equivalent full-time work. In the above-cited background study, Kesselman argues that subsidies for private sector employment could be in the rage of $1.50 - $3.00.

Clearly, there is room to shift expenditures at no net budgetary cost, or even at a saving. The trick is to find the expenditure channel that will entice

Canadian employers to create new jobs. Doing so is not simple, but neither is it impossible. And ultimately, the economic costs and social injustice involved in not addressing the problem at all are unacceptably large.

NOTES

1. "Comprehensive Income Security for Canadian Workers," in *Income Distribution and Economic Security in Canada*, F. Vaillancourt, Research Coordinator (Toronto: University of Toronto Press, 1985).
2. See, for instance, Cook et al, *Economic Impact of Selected Government Programs Directed Toward the Labour Market* (Economic Council of Canada, 1976); Layard and Nickell, "The Case for Subsidizing Extra Jobs," in *Economic Journal*, March 1980; and Whitley and Wilson, "The Macroeconomic Merits of a Marginal Wage Subsidy," in *Economic Journal*, December 1983.
3. A brief discussion of this point is available in the Dodge Report. See Employment and Immigration Canada, *Labour Market Development in the 1980s* (Ottawa: Supply and Services Canada, Ch. 7, 1981).
4. R. Tannenwald, "Are Wage Training Subsidies Cost Effective?", *New England Economic Review*, September-October 1982.

DISCUSSANTS

Monica Townson — Economic Consultant

It is worth repeating that we are mandated to investigate policies for *full* employment. Economists can argue about what constitutes full employment, but there is no getting away from the fact that four years after our economy started to pull out of recession, unemployment stood at nearly ten per cent, with over one million Canadians still out of work. Those are seasonally adjusted figures, and they only reflect the officially unemployed. A simple definition of *full* employment would be that there are jobs for everyone who wants to work, and who wants the wages that go with that employment.

Much of Frank Reid's paper is based on the premise that people would be willing to give up wages in return for a reduction in working time, and that this would create employment opportunities for other workers. The assumption that workers would do this voluntarily is based partly on a 1978 U.S. survey. I think that it would have been interesting to have more information about the survey, and about the workers who took part in it. Were they male or female, for example, and did the women respond differently from the men? Was there a difference in response according to the income level of the workers? I suspect these factors might have a very important bearing on the responses to the survey. If it is true that workers would be willing to reduce their hours and take a cut in pay at the same time, why don't they do it? Why don't workers take unpaid leaves of absence, or switch from full-time to part-time work?

Mr. Reid points out that employees who do so "may suffer financial penalties, such as lower wage and fringe benefits". That, of course, is the point of the matter. A policy that enforces reduced work time and reduction of pay, the kind of policy that certain European countries have implemented, obviously has a very severe impact on *lower-income* workers. I believe that is the major drawback in this proposal.

Mr. Reid's paper looks at a reduction in working time as a potential temporary measure to redistribute work during periods when there is deficient-demand unemployment. In fact, he expresses concern that unions that negotiate work time reductions might regard them as permanent contract improvements. Personally, I am all in favour of that. Reduction in work time in the past hundred years has been accomplished through the persistence of unions. Interestingly enough, the first strike for shorter working hours took place in 1791, when journeymen carpenters in Philadelphia walked out. Their goal was a regularly scheduled day from 6 a.m. to 6 p.m.

Unions in Canada today are also pressing for a shorter work week, but as Mr. Reid points out, they want to shorten it without loss of pay. Such a proposition would be feasible, especially if shorter working hours bring

increased productivity. When Reid characterizes this demand as equivalent to asking for a 14 per cent hourly increase in pay, his calculation ignores the impact of such a reduction on productivity. The paper does point out that there have been productivity increases in the European countries, where shorter work weeks have been implemented. That, of course, means the impact of the shorter work week on increasing employment is not as great as might have been expected.

Some of the European countries have succeeded in increasing employment through a combination of measures. For example, West Germany was able to generate about 800,000 new jobs through a shorter work week, flexible retirement options, paid educational leave, lengthening annual leave, increasing part-time work, and extending the school leaving age. Obviously, some of these options are more attractive than others.

Reid's paper does not examine the possibility of flexible retirement options, an option that I think might hold some promise for Canada. We might examine the phased retirement program under Sweden's pension scheme where a worker may retire early, work shorter hours through the week and begin to draw on the state pension to compensate for the loss of pay. Such options, which do not involve any financial penalty for the workers, offer the best potential for combatting unemployment through reduced working time.

The paper does deal with short-time compensation, or work sharing as it is called under the unemployment insurance program, and as Mr. Reid points out this program has been costly. Most of the workers who have benefitted from the program are men. In 1982, for example, 77 per cent of the participants were male. Hugh and Pat Armstrong have identified the same problem with other federally-funded job creation programs. The unemployment problem as it affects women was not mentioned in either of the papers in this section. I raise it here because I think it is very important. So many of the labour market studies done by economists are based on the prime age male worker model, yet there are more women in the work force than prime-age males. I think we have to be very careful to recognize this when we are devising strategies to promote full employment.

We also have to recognize that occupational segregation by sex remains a fact of life in the Canadian labour force. Women workers are confined to a very limited number of occupations, which explains why work sharing programs have done so little to help women. It may also mean that reduced working time strategies will not have the impact we expect. This issue is not addressed in Frank Reid's paper.

Perhaps the most significant impact of reduced working hours is the possibility that parents will be able to spend more time with their children. In the majority of families with young children today, both parents work. Yet we still cling to existing arrangements and working times designed to meet the needs of the male worker, who has a wife at home to cook his meals, wash his clothes and look after their children. Very few workers now fit that

model, since 43 per cent of our work force is female. A shorter working week would facilitate the sharing of domestic labour between woman and men. Need I point out that, until such sharing happens, women will not achieve equality.

I firmly believe that the shorter work week has got to come, and I firmly believe it can be done without loss of pay. But I am not convinced at this point that it will have a major impact on employment, unless, as Frank Reid points out, we have a substantial reduction in the work week to something like 35 hours or even 30 hours. I believe Sweden has identified this as a serious goal, but I think it is a long-term proposition that cannot be achieved if workers are forced to give up badly-needed income.

The paper by Arthur Donner and Mel Kliman does a very good job of outlining the pros and cons of wage subsidy programs, but I found the cons much more convincing. For example, as the paper says, employers may apply for subsidies to create jobs that would have been created without the subsidy. If the subsidy is attached to the worker, as the Macdonald Royal Commission recommends, that worker may simply be subsidized into taking a job away from someone else. There is no guarantee that a subsidized job will end up being a permanent job, unless the worker can get some kind of training during the subsidy period and get something better at the end of it, assuming that better jobs are available then.

The Thatcher government in Britain has been using this kind of program to deal with youth unemployment. Under the British Youth Opportunities Program, and the Youth Training Scheme which succeeded it in 1983, young people who leave school at the age of 16 or 17 are placed with employers and receive a weekly allowance from the state. Employers also receive an allowance for providing courses in job preparation. But according to one estimate, only about 20 per cent of young people who participate in these schemes ever get a permanent job in the end. Even right wing economists admit that the program is "little more than a free pair of hands for employers". This is the danger of wage subsidy programs.

If the non-accelerating inflation rate of unemployment or NAIRU is really in the 6.5 to eight per cent range — assuming that there is such a thing as a NAIRU, which I think is itself questionable — and if wage subsidies could indeed be used to help those workers who are still without work when the unemployment rate is at NAIRU, it is very clear that those workers will come from disadvantaged groups. With wage subsidies, employers will be able to hire them at even less cost than they do now.

The paper correctly points out that reducing NAIRU is a matter of changing the structure of the labour market. But how is this to be done? Policies such as employment equity, for example, which are designed to break down the systemic values that reinforce occupational segregation, are met with howls of protest from the business community. The Canadian Federation of Independent Business claims that the unemployment insurance program has had

a devastating impact on employment, and particularly on small business hiring. They say at the same time that small business has been the biggest source of job creation in the Canadian economy. Which of these statements is true? They cannot both be true.

The Macdonald Royal Commission's prescription for cutting unemployment insurance benefits is based on an analysis of the impact of U.I. on the labour market that is more than 10 years old. The studies that the Commission quotes to support its thesis that a generous U.I. program has increased the measured unemployment rate were conducted in the mid-1970s when unemployment was below seven per cent and the number of Canadians out of work was half of what it is now. The Donner-Kliman paper refers to the Macdonald Royal Commission's proposal for a transitional adjustment assistance program, whose goal seems to be to get workers to move around the country in search of jobs. Once again, the economists at the Commission propose a solution that might fit the prime age male worker, but it probably would not work at all as a solution for female unemployment. And one must question a strategy that tries to move workers rather than creating jobs in places of high unemployment.

Donner and Kliman make it clear that wage subsidies are being discussed because, "in the present political environment in which broadly based expansionary fiscal and monetary policies and growth in the public sector are anathema to government, wage subsidies become more attractive". Even if equal or greater job-creating potential can be found in other policies, they note, the fact that wage incentives are directed to job creation in the private sector makes them politically acceptable. While cutting back UI benefits to get those lazy people back to work again, we are handing over money to business so they can operate at lower cost. This is an approach that I have some trouble with. The case for wage subsidies is not clear-cut, and they are no substitute for the management of aggregate demand.

Keith Newton — Economic Council of Canada

Frank Reid's paper is very clear and concise, although if one really wanted to quibble one might say that the available evidence on this particular set of policies is really not all that convincing. My reading of the European evidence is that the employment creating potential of work time reduction policies has been offset by increases in productivity. My major problem both with the Reid and the Donner-Kliman paper is that there is not much information about what has happened in Canada. On the question of employment sharing, perhaps I could add something to what Frank Reid mentioned about recent Canadian research.

The Conference Board in Canada recently undertook a survey of attitudes to reductions in working time. A series of supplementary questions was attached to the labour force survey, and about 30,000 households were

questioned. The respondents were asked, first, if they would trade pay for more leisure. Second, they were asked whether they would trade portions of anticipated future pay increases for more leisure. Other questions related to the pattern of preferred reduction in working time — reduced hours per day, fewer days per week, fewer months per year, special leave, or early retirement. There were also questions on what people would do with the increased leisure time. Responses were coded by a variety of characteristics — sex, age, income, education, family size, union membership, etc. The survey was conducted in the summer of 1985, and tapes of the results should now be available from Statistic Canada.

Donner and Kliman sound apologetic about proposing wage subsidies as a possible contribution to the reduction of unemployment. I am not completely convinced of their usefulness, but I will try to expand on the justification for such a policy as one of the options for full employment.

A first consideration is the diagnosis of the unemployment problem, as it is set out in the overview paper by Sharpe, Voyer and Cameron. They point out that while many unemployment spells are short-term, and can be addressed by a variety of measures to improve the matching of jobs and workers, a significant share of total unemployment involves much longer periods of joblessness for particular groups in the labour force. A second, related concern is whether recourse to conventional macro-economic instruments to ease unemployment would lead to unacceptable rates of inflation. Third, since long-term joblessness is borne by relatively few people, there is an important equity dimension to the unemployment problem, that suggests a need for an approach that is more finely targetted. As Donner and Kliman note, perhaps one of the main justifications for wage subsidies is precisely the fact that they can be targetted.

The single most important message I draw from their paper is that wage subsidies must be part of a coordinated package of policies. Wage subsidies are not a substitute for management of aggregate demand. The authors did not point out that Canada has experimented with a number of direct job creation policies over the years, including wage subsidies. It is a bit disappointing that Donner and Kliman do not give more evidence of the success of such programs. Most of the recent studies they cite are British or American.

In fact, there is some research available for this country. It was undertaken by my own organization, the Economic Council of Canada, in the early 1980s. Some of the results were published in *In Short Supply*, a Council study that focussed on the employment tax credit program, a form of direct job creation through wage subsidies. There was also a very detailed and systematic piece of work on this subject that was used as background by the Council. It is authored by Surendra Gera, as part of a Ph.D. study at Carleton University.

One of the concerns that Donner and Kliman raise about the incrementalism of employment creation subsidies is in fact a very important consideration.

The study shows that only about 30 per cent of the employment created is in fact a net improvement. It estimates that the cost per job of a wage subsidy program in 1979 was about $17,500. Finally, I want to add to Monica Townson's point that new jobs should be created as a result of wage subsidies, not simply windfall payments to employers. The Council study seems to indicate that the windfall element, for employers, amounts to between 63 and 80 per cent of the entire subsidy, which is obviously a major concern.

Terrance Hunsley — Executive Director, Canadian Council on Social Development

My theoretical framework, or as some would have it, my persistent bias, is that not all citizens in Canada are assured an acceptable quality of life, nor is that quality evenly distributed. Income distribution data show that, over the past four years, the bottom four quintile groups or 80 per cent of families have suffered real income losses, while the top quintile has increased its real income despite the recession. The growing number of soup kitchens and food banks is an ever more obvious indicator of the extent and nature of the decline in quality of life for many Canadians.

An analysis of the concept of full employment and the ways to achieve it poses certain obstacles. For example, we lack a shared concept of what full employment means. A second obstacle is ambiguity over the types of behaviour and institutions that are desirable or undesirable. For example, Gilles Paquet in his comments brought up the question of rigidities. I attended a Conference Board seminar where it was suggested that if we could only reduce or eliminate rigidities, we would be better off. When you ask about these so-called rigidities, you are told they include income support programs, minimum wages, labour standards, pensions, and medicare. But are not these programs essential to the maintenace of a certain amount of equity within Canadian society?

Regarding the Macdonald Commission, I am not reassured when I hear from the Chairman that we do not have to worry about our social programs being on the table in free trade negotiations because the Americans have to put their programs on the table as well, or that we would not have to reduce our programs unless the Americans reduced theirs. On the other hand, I do not think we should be frightened by the Macdonald Commission. What it has done is bring to public debate a wide range of important issues on the relationships between income support programs, taxation, and trade and industrial policy. This is beneficial for Canadians. The re-introduction of the concept of the guaranteed annual income for public discussion is also to be lauded. It is interesting to me that 10 to 12 years ago, when the Canadian Council on Social Development published a book on guaranteed annual income, it was seen as a social measure. Now it is presented as an instrument for economic adjustment, to ease us through the transition to a more internationally competitive economy.

My working hypothesis for this discussion is that, in our mixed economy, the private sector will not be able to create enough jobs, within the time frame we would judge acceptable, to meet any type of full employment objective. Consequently, public intervention is necessary. This means we must manage the distribution of opportunities and provide income support to individuals and groups. The Canadian Council on Social Development has stressed the role of public investment in fostering the growth of local economic initiatives. In addition, we have suggested that the public sector must promote direct job creation by providing more community-based services, funding public infrastructure, and providing work redistribution.

Turning to the papers, the idea of bringing about a voluntary reduction in working time by modifying the present structure of available choices and opportunities is a good one. However, it would only be effective if large amounts of time were involved. As Frank Reid points out, reducing the work week by a half-hour would result in increased productivity, but would have only a limited effect on employment. I think we should stress reduction in the work year (by working fewer weeks), or in the total number of years in one's working life (by earlier retirement), over reduction in the average work week. Increased voluntary reductions in work time may pose problems for women, so appropriate protection would be required in any legislation.

The federal government has announced major cuts in person-years in the public service (12,000 person years by 1990). Rather than cutting back, the government should have looked at ways of avoiding layoffs through work sharing (particularly among higher paid employees), such as reducing the work year from 12 to nine months. This could have the effect of increasing employment.

I think the Reid paper could have been strengthened by exploring the possible social and economic benefits of increased flexibility with respect to equitable child care benefits. For parents, the social benefit of a change in work-time patterns is important. But the economic benefits for society, through the creation of an expanded day care system, could also be considerable.

Turning to the Donner and Kliman paper, I do not see a wide application for wage subsidies. While wage subsidies can be very useful in achieving affirmative action objectives, I think their broader application is limited. First, such a program has the potential to distort private business decisions. Second, as was pointed out, it is very hard to measure the impact of wage subsidies on employment, since any increase in employment following the introduction of a wage subsidy program might have happened anyway.

The Macdonald Commission is proposing the Transitional Adjustment and Assistance Program to reduce transition costs for workers affected by structural changes in the economy. But it is still workers and not businesses who are bearing the cost of change. Maybe the costs should be transferred to business. The TAAP program also assumes that Canadians are mobile and

should be mobile. But what about the economic and social costs of that mobility, such as the new social costs in areas of rapid growth, the higher service costs in areas that are losing population, and the overall impact on families? When we talk in terms of a more competitive society, we must look more deeply at the social consequences of such a society.

Donner and Kliman state that there is a general consensus in Canada, as shown by public opinion polls, that inflation must be kept under control. The problem with governments responding to this supposed consensus and making inflation control their number one economic goal, without regard for the effect on unemployment, is that public opinion interviewers do not give the public adequate information on which to make policy choices. If the public had known the high cost of reducing inflation in terms of increased unemployment, it might not have given such a high priority to inflation reduction. Indeed, the rise in unemployment in the 1980s quickly changed public opinion on whether employment or inflation is Canada's major economic problem.

Political Analysis of Policy Proposals

All political parties attach great importance to job creation. In this section, representatives of each federal party present their views on full employment and economic policy. Lloyd Axworthy (L-Winnipeg-Fort Garry), Jim Hawkes (PC-Calgary West), and Lorne Nystrom (NDP-Yorkton Melville) have had responsibility within their respective parties for employment matters. A common theme that emerges is the importance of local and regional considerations in the making of employment policy. Axworthy stresses industrial policy, Hawkes explains how Parliamentary input into policy debate has changed as a result of the reform of the committee system, and Nystrom presents the conclusions of the New Democrat task force on job creation.

Lloyd Axworthy

Liberal M.P. and Trade Critic,
former Minister of Employment and Immigration

The full employment question strikes me as an interesting contrast to the sessions at the 1985 Federal-Provincial First Ministers' Conference in Halifax. In Halifax, I did not hear the term full employment mentioned once. This tells us something about political priorities in this country, and about the attention recently given the goal of full employment, a policy objective which was first adopted in 1945. At the Halifax conference there was much rhetoric about growth and expansion, but not once was a specific employment or unemployment target put on the table by the first ministers of this country.

This should not come as a great surprise, because we have seen full employment fade from public view in the course of a number of economic shocks in this country over the last couple of decades. Perhaps more important is that there has been a loss of confidence in the ability of government to bring about full employment. I think this confidence problem is linked to a general disillusionment and frustration within governments. The strong sense of public confidence that encouraged full employment positions that were taken by most Western industrial countries after the Second World War has been undermined by seemingly intractable problems that arose in the 1970s. Our vocabulary and, more important, the economic and social agenda that goes along with it, have changed substantially.

My first comment has to do with political will, and how full employment gets back on the political agenda. Full employment is more than just a technical question. The real problem is how to establish the concept of full employment on the political agenda — once there is some agreement on what it means — and focus the debate on how to achieve it. Part of the problem in establishing full employment as a political priority in this country is to have a much clearer sense in our minds as to the role of government in the equation. Even the strongest proponents of state action find themselves apologizing when they call for it. They are subject to attacks from neo-conservatives, from the new economic wizards in our think tanks, from the combined coalition of business organizations, and other "deep thinkers" of our time. There has been a clear victory for the coalition on the other side of the full employment issue, largely because people have become convinced that government cannot act to achieve full employment.

Several of the papers point out that unemployment is in part dependent on external factors, such as the level of economic activity in the United States. This has caused people who see room for positive and constructive government policy to do some serious rethinking about how to respond to unemployment and to establish a different set of goals on how to achieve full employment. But we still have a long way to go. We also need to come to grips

with the growing dichotomy between economic growth and job creation. Again, one of the problems with the debate that took place in Halifax was the complete preoccupation with economic growth. There was virtually no consideration of how to distribute the benefits of that growth, to ensure that we end up having employment evenly distributed across Canada.

One thing I learned as Minister of Employment and Immigration was that it wasn't enough to simply talk in aggregate terms about unemployment. It takes an understanding of a wide variety of causes and conditions. Even in 1981, when the unemployment rate was seven per cent, there were still very deep pockets of unemployment in a number of rural areas, in specific regions of Canada, and among certain groups. In Manitoba, the native population has never seen unemployment less than 40 to 50 per cent, yet the native population currently accounts for 20 to 30 per cent of the growth of the labour force in Western Canada. Consequently, we can't just talk about creating an environment of growth at the macro level. Without special programs that target the very specific pockets of unemployment and alter the conditions that cause that unemployment, real problems will persist.

Some economic growth may be counterproductive to society if it creates wealth but eliminates jobs. Indeed, the creation of additional wealth is only a positive factor if that wealth is redistributed in such a way as to create jobs where they are needed. The only government leader who came close to expressing this view at the Halifax First Ministers' Conference was Premier Brian Peckford of Newfoundland, who pointed out that there are large parts of the country where a job strategy based on the private sector would not work. In some areas the private sector is too thin; in other areas it does not exist. Therefore there have to be concerted efforts and investment by government, just to ensure that there is useful activity available for individuals. And this reality, the inability of the private sector to create sufficient employment, is not just limited to Newfoundland. There is not one region or province in the country, including Ontario, where we see sufficient employment opportunities. I am sure if you go to the downtown core of any Ontario city, or to Winnipeg, Vancouver, or Montreal, you will find that unemployment among young people, certain ethnic groups, and single mothers is unacceptably high. Therefore, while a public policy for economic growth is necessary, the tough question is how to make sure that the fruits of economic growth are equitably distributed among Canadians.

Based on my recent calculations, if we accept the argument that you can increase the return from current macro-economic initiatives, and that means adopting policies that give more jobs from current deficit spending, we are still probably talking about a minimum seven per cent unemployment rate. Let us be generous and say that, before 1990, we will see full maximization of those kinds of demand factors — even then, you would still be at seven per cent unemployment. This means that we could create about 1.7 million jobs between 1985 and 1990 if we maintained a growth rate in the three to 4.5 per cent range. However, given labour force growth of about 1.3 million, if we

aim for a five per cent unemployment rate, which is closer to the full employment standard I would establish, there is a gap of about 400,000 jobs. Even if we maximize our efforts on the macro-economic front, there is still a shortfall of jobs for new entrants to the labour market. The key question is how to generate those extra jobs. What tools, what instruments, what initiatives can be introduced to try to achieve that goal?

We should begin by admitting that unemployment is both a supply and demand problem. We have to generate jobs in our industrial sector, and at the same time substantially improve our labour market performance. On the industrial side, without over-simplifying, our 300 to 400 industries can be divided into four major categories. First there are the star performers, those industries that have a high level of growth and a high level of export performance. One example is the auto parts industry; others are to be found in the natural resource exporting industries. Then there are the under-achievers, those 30 to 40 industries which have a job creating capacity that is not being met. These industries do not reach their potential for a series of complex reasons. For some, it is an inability to raise capital, a problem that is especially significant for small business. For others it has to do with the regulatory environment and the tax system, that is to say that failure to achieve their export or employment potential can be traced to constraints imposed upon them by the regulatory, tax, or international trade support system. In my third category I would put the mature industries; those industries that are now under intense competition from abroad, and have problably reached their maximum growth potential. Good public policy could ensure that they do not deteriorate. While they do not have potential for job creation we could see some stability in their employment levels. The fourth category, often called the industrial losers, are those industries that in kinder language must undergo significant adjustment. These industries face an incredible amount of change in the markets that they serve and in their labour force. In order to survive they require substantial assistance.

I think that over the five-year period, with the right mixture of industrial policies, and by that I do not just mean grants or subsidies, but regulatory, capital investment, tax and export programs targeted to each of those four categories, we can make considerable progress. For the first category of industries greater growth can be achieved; for the second category more potential can be met; for the third stability can be maintained, while for the fourth job losses can be minimized. The appropriate policies will differ by sector and even within sectors. A well articulated industrial policy based on the realities of each and every sector is absolutely essential to support any trade initiative with the United States if we want to minimize the negative impact of such a policy on employment in Canada and achieve full employment. There is simply not one set of policies that can be applied everywhere. The super successful firm may still need help, but not the same help as a mature industry. What bothers me about the trade initiative is that it seems to tie us into serious restrictions on industrial policy. At best it would leave us with

only one acceptable comprehensive policy. And that could well mean applying the wrong solutions to the wrong industry at the wrong time.

Turning now to the labour market, I am convinced several very important initiatives can be taken. Indeed I am speaking from experience. Not only was I a Minister of Employment and Immigration for three years, I weathered the 1981-82 recession. The recession actually forced us to produce innovative programs, showing the truth in that Chinese expression, that "crisis begets opportunity". I would say that the most important thing to recognize is the absolute necessity of a high level of federal government investment in labour market programs. The idea that you can pass off such investments to the private sector is foolish and is one reason why the current government's job strategy is so far an unmitigated disaster in terms of job creation. It is not working in many areas of the country because it has simply not met the need for specific labour market policies in these areas.

There must be a high level of not just traditional investment but also of highly innovative investments. I will give four or five examples. First, let us take the case of the Winnipeg Inner-City Project. The impetus for this project did not come from the local level. Rather it was a decision by the federal government to approach the city of Winnipeg and the Province of Manitoba with a proposal to develop a program targetting the inner-city unemployed that got things started. The Winnipeg project acted as a blueprint for the integration and consolidation of a large number of federal programs aimed at one specific geographic area, in partnership with other levels of government. The notion of having a tripartite policy committee, with management at the political level by the mayor, provincial minister and the federal minister of regional expansion, provided a high level of flexibility in the program and enabled us to target specific groups.

This type of initiative could serve as a model for other cities with similar problems. Indeed, I think one area in which the federal government must take a new approach is its involvement in urban problems. The Liberal government disbanded the Ministry of State for Urban Affairs because it was not working well. But the idea that cities are off limits to the federal government is nonsense. There is a great capacity for federal investment, using the city as the agency of delivery, to deal with employment problems. The paper by Penina Coopersmith addressed this issue very well. I think we should look at how we can transfer more federal dollars to the cities.

Another initiative was the local economic development corporation, or the LEDA program as it became known. In 1982 we instituted LEDA as an experimental program and established 15 experimental local economic development corporations. The idea was very simple. We gave seed money to local economic groups so that they could form a corporation. They received sufficient funds to do marketing studies and organize themselves. We then provided $250,000 for equity financing. The tracking we did of their operations up to 1984 showed them to be very successful. I can cite an example from

my own province. A consortium of six tribal reserves in the southwest part of Manitoba created 27 new businesses ranging from local gas stations to an archery equipment factory producing for the export market. Federal money helped the tribal council lever private capital. But it was the local community that set the priorities and established the program. There is a great opportunity for similar local economic development corporations to create employment where the private sector is undeveloped. We need a national organization to provide technical assistance as well as funds for local economic development. Such a development bank should have been established in the 1980s. A similar proposal was put forward by the Dodge Task Force on Labour Market Development, but unfortunately I was unable to sell it to Cabinet.

On the skills development side, many things can be done. First, I think the unemployment insurance program should be transformed into an employment insurance program. One of the major components of such a program would be a skills development program, in which employees, employers and the government would contribute to a fund to finance long-term worker training in anticipation of job transition and industrial adjustment. Such a program would allow workers to take time off for retraining, and allow Canadian society to meet the need for large scale upgrading of skills. On this topic, I can recommend the task force reports on skills development that were published by Employment and Immigration in 1984. These studies did not assume a high level of cooperation and agreement between the business community, labour, and the federal government in working out the specific formula for a skills development leave program, but I think that would be needed.

I would also like to point out that a major skills development leave program could take about 100,000 workers a year into educational training programs. Such a program could go a long way in meeting the goal of reducing unemployment to five per cent by 1990. By recycling about 100,000 workers into educational training programs each year, we not only ease the pressure on the labour force at any point in time, we also help 500,000 people over a five-year period prepare for new labour market opportunities. This could be done through using the U.I. system.

The other area that deserves priority is literacy training. This has been seen by some as a provincial matter, and the federal government has been nervous about getting involved. For example, there is nothing in the current government job strategy to address the problem of illiteracy. Yet there are about 1.2 million individuals in this country who are unable to read or write, for whom illiteracy represents a most serious barrier to employment. Canada has a number of under-used educational institutions, particularly at the primary and secondary level, that could be brought into play. The Winnipeg Core Initiative identified literacy as a major problem for native people coming into the city and attempted to upgrade their educational level from Grade 7 up to Grade 11 or 12. There is no coordination in attacking this issue because it is

unclear which level of government has primary responsibility for basic literacy training for adults, but I do not accept this as an excuse for inaction.

Another policy area where action is needed is youth unemployment. A guaranteed youth employment program is the only way that many young people can obtain the kind of work experience they will need to land permanent jobs. Diane Bellemare and Lise Poulin Simon discuss the important role of national apprenticeship programs in European countries. These programs use wage subsidies to induce both profit-making and non-profit employers to give a young person job experience combined with some institutional training. This type of program would cost about $1 billion per year, but it would be well worth the expense to get our young people into the job market.

Another program that would reduce unemployment is work sharing. In 1983, there were close to 300,000 workers on work sharing schemes financed through the unemployment insurance system. This type of scheme can be seen of as a sort of job insurance, in that it did prevent layoffs for many Canadians. I should point out that, although work sharing was opposed by the union leadership when it was introduced, local unions rejected the advice of their national colleagues, and we eventually got labour participation in the program. Additional work sharing programs could be promoted, using provisions of the Unemployment Insurance Act, in order to facilitate industrial adjustment. Like the skills development leave program, work sharing could provide an opportunity for people to be retained on a part-time basis and hence avoid future job dislocation.

In my time as Minister of Employment we had some experience with the use of early retirement to reduce unemployment. Our department developed the Industrial Labour Adjustment Program (ILAP) to target resource industry towns that had lost their main source of employment. I think early retirement benefit programs need an income security component to give a real incentive to people aged 50 or 55 and older to leave a job. But there should also be an equal or complementary job creation component to the program. One of the ideas that was discussed in 1983-84 was a national volunteer service, in which people would receive their early retirement benefits but would also work part-time in social service areas where community needs are not being met. Such volunteers might also receive an income supplement.

If some combination of the industrial policy and labour market programs outlined here were brought together, the gap of 400,000 jobs that will be there under the best of circumstances by 1990 could be erased. We could then look with some degree of assurance at having a five or six per cent unemployment rate, which is a lot better than what we are looking at now.

Jim Hawkes

Progressive Conservative M.P.,
former Chairperson of the Standing Committee
on Employment and Immigration

I represent the Government of Canada and the Standing Committee of the House of Commons on Employment and Immigration. I have a deep conviction, and I think it is shared in our caucus, that my party won the last election because the Canadian people wanted something different. They wanted better financial management and they wanted more jobs. We may or may not be able to do it, but I think our chances of re-election are directly related to those two variables. Will we manage the finances of the country better, and will we create more jobs?

The current Parliament is very different from the previous one, and perhaps from all other Parliaments in the last 50 years. A major difference, and I say this with tongue in cheek, is that there are fewer lawyers and, to my knowledge, no economists. What you have in the Parliament of Canada today, in increased numbers, is Parliamentarians whose entire background, prior to the election, was in the area of owner-operated small business. Their attitudes and mentalities have been shaped by this life experience. The policies that result from this background, I suggest, will be different from past policies.

We can already see the results. The press and the country are nervous because there does not seem to be any grand design to policy, and we have been accustomed to grand designs. However it is not the nature of small businessmen to think in terms of grand designs. Rather, it is their nature to tackle real problems, concrete problems, and solve them one at a time. I think public policy is beginning to reflect this approach, even though it is an approach that is not yet understood.

Let us turn to Parliamentary reform, and my role as Chairperson of the Standing Committee on Labour, Employment and Immigration. Historically in this country, it has been the job of Cabinet to propose public policy, and of Parliament to dispose of it. Cabinet ministers have relied on public servants to generate ideas and provide technical advice. As of January, 1986, the standing committees now have the power to propose new policies. These Parliamentary committees will conduct their own inquiries and determine their own terms of reference. For the first time, standing committees will have power to hire permanent researchers. We will, in effect, be moving closer to the American model. Parliamentary committees will be able to propose departmental budgets to the House of Commons as well as legislation. These committees will serve as a check and balance to the Cabinet and bureaucracy, the two bodies that currently wield the power in the Canadian political system. You can expect some conflict as a result of this. Out of that conflict will come new creativity as well.

I would like to turn to a theme that Lloyd Axworthy stressed, a theme which runs counter to the approach of the current government. This theme is familiar from the Trudeau years, a concern with central planning and decision-making. In his discussion of the Dodge report and its recommendations for federal funding of local development, Mr. Axworthy mentioned a national agency. In contrast, the Conservative caucus talks of regional agencies, and in general terms of decentralization or regionalization of public policy instead of centralization.

On the issue of full employment, there is a deep conviction in our caucus, and this is reflected in our policy processes, that the status of labour in this country is one of the reasons for unemployment. It is the lack of adequate skills and training on the supply side that is a root cause of some of the unemployment.

Lloyd Axworthy mentioned that 10 per cent of the labour force in Canada is functionally illiterate. This situation is an illustration of the supply-side nature of unemployment. Given the rapid rate of skills obsolescence due to changing technology, the lack of basic skills in our work force represents an even more serious problem. The solution to this problem is education.

In the past, social spending has been essentially an income support mechanism, whether we are referring to unemployment insurance or the Canada Assistance Plan. I think we must now move to a different approach to social spending, as investment expenditure in human capital. This would be a more effective and efficient use of a large portion of these dollars.

Lloyd Axworthy mentioned that we should institute training insurance. I made my first speech to the House of Commons on the Crosbie budget in 1979, and at that time recommended replacement of unemployment insurance with employment and training insurance.

Along with greater stress on investment in human capital, there is a need for more local control over decision making. Geographically, we are the world's second-largest nation, yet our population is small relative to our size and it is a diverse population. If we are going to make efficient public expenditure decisions on the supply side, we must allow more local control. The main feature of the Canadian Jobs Strategy is that a variety of employment creation and training projects have been brought together under a much more flexible policy framework. The best example of this policy orientation is the creation of local advisory councils which will develop training and employment programs to meet the specific needs of the communities they serve. Local people will have control over spending and policy. This represents a change in philosophy about public spending.

I think our manpower policy has been mistaken in its emphasis on national imbalances in labour supply, in its concern that we are short so many carpenters and plumbers. The country does not work like that. We should be

thinking in terms of local labour market needs, giving individuals more choice, and retaining less public control.

I also think we have gone as far as we really should go with public sector education. The emphasis for the next few decades should be on private sector education. There should be more educational facilities available from private sources, and more training should be taking place in the workplace. Indeed, firms should think of themselves as educational institutions whose interests are best served by the development of their human resources. This has been the European approach, and I think a move in that direction would be positive. On the same subject, I believe Canada is in a position to market educational material to the world. Knowledge-based industries represent employment opportunities, both national and international, and we do have a lot to offer.

In addition to the supply side policies already discussed, the government has made a solid attempt on the demand side to restore consumer and investor (domestic and international) confidence in this country. The emphasis on expenditure and deficit reduction is based on the belief that success in this area will change Canadians' psychology and create greater demand. A reduced deficit will lower interest rates. The May, 1985 budget injected $2 billion into the economy. Through changes in the RHOSP program, people were able to use their savings for purposes other than home purchases. They were given more freedom to spend. The much-criticized capital gains exemption is a signal to the Canadian people that the government wants them to invest rather than save. The trade initiative with the U.S. is also aimed at increasing demand by expanding markets in the United States and thwarting protectionist policies south of the border.

One factor which is generally ignored in the debate about employment policies is demographics and, in particular, the age structure of the population. Indeed, the drop in the birth rate since the mid-1960s and the shrinking proportion of the population under 20 constitutes a major weakness in the Canadian economy. If the birth rate had not fallen, at least 250,000 more Canadians would be employed today to meet the demands for goods and services from that larger number of children. We tend to think of the falling birth rate as affecting the size of the labour force with a 15-to-20-year lag. But one of the causes of unemployment today is that we have too few children. Children are not competitors in the labour markets, and they are good consumers.

We have a shortage of small businessmen in this country, and if you look at the age structure of the population, you will find a shortage of people between the ages of 40 and 55, the most common ages for starting a small business. It is the time in life when one has the required experience, the capital, and the ideas to start a new business.

These demographic realities suggest the need for changes in immigration policy. In contrast to the 1982 policy, which reduced target immigration

levels, this government plans to increase the target level. It is the government's view that increased immigration, and therefore increased demand, is good for the country. I predict that, by the end of our current term in office, Canada will be admitting at least 200,000 people a year and possibly more. Without more rapid population growth, Canada will have trouble moving towards full employment.

Lorne Nystrom

New Democrat M.P. and Deputy House Leader

In Canada we have an unacceptably high official unemployment rate of nearly 10 per cent, though we know it is far higher when we take account of people who have dropped out of the labour force. I recently co-chaired a federal New Democrat caucus task force — known as the Action Group in Jobs — which held community forums in 24 centres from coast to coast and met with some 500 organizations and individuals to explore job creation alternatives. We found that real unemployment rates were higher than 30 per cent in many parts of the country, and that such high rates of joblessness were responsible for many individual stories of dislocation and despair. More surprising, we found that ordinary Canadians remain optimistic about their capacity to build on our economic potential at the community and national levels, and that many communities have already begun to explore new alternatives.

A theme expressed many times in presentations to the Action Group on Jobs was the demand for more local control over decision making. People were skeptical of strategies based on corporate megaprojects and "top-down" central planning. People want more money and more power, to make decisions over their own lives in their own communities.

Recent years have seen a rapid growth of new institutions such as worker cooperatives, community development corporations, and municipal enterprises at the local level. People have learned that they need to build on their local strengths, rather than relying on large corporations for jobs. But they have also learned that government support in the form of funds, expert assistance, and legislation, such as measures to give workers the first right to purchase assets when a company fails, is vital if local initiatives are to succeed.

That is why we have proposed a major Community Initiatives Fund, as well as new legislation to secure more democratic economic decision making at the levels of the enterprise and the community, particularly in single-industry, resource-based communities. Expenditures to assist these local initiatives could, we determined, be paid for by scaling back unproductive tax incentives to large corporations which have failed to create the jobs we so badly need.

The second major thrust of our report was to call for a greater measure of national self-reliance and self-direction, in areas ranging from control of our own interest rates to greater control of foreign investment, and a diversification of our resource-based economy through measures to upgrade export processing and promote more secondary manufacturing to meet our domestic needs. We noted in our report that government leadership is necessary to counter both corporate and foreign control of our economic future.

I, personally, am a product of the CCF and the cooperative movement in rural Saskatchewan, which I think has some lessons for all Canadians. The farmers were forced to band together and create a cooperative movement to save their farms. They formed wheat pools, which are still farmer-controlled and owned and handled 66 to 75 per cent of grain sales. Farmers also formed credit unions, grocery stores, and other cooperative endeavors. In Yorkton, Sask., you can do business at a co-op pharmacy and a co-op hardware store, and even eat at two co-op restaurants. These local initiatives helped take Saskatchewan from being one of the poorest provinces, to the national average in terms of income.

In tandem with the co-op movement went a tremendous expansion of public ownership. Saskatchewan has a large publicly owned sector — auto insurance, potash, and oil wells — in areas where co-op control would not be feasible. This has created jobs and kept people and money in the province, while retaining provincial control of our resources.

Until recently there were nine Saskatchewan companies mining potash, all foreign owned except for Canadian Pacific. Then the government created the Saskatchewan Potash Corporation which controls about 40 per cent of potash production. With a head office in Saskatoon, management jobs are available locally instead of in places like Dallas. Research and development jobs are located in Saskatchewan. I think this shows that public ownership is an appealing option, especially in parts of the country where the private sector is weak or non-existent.

In the final analysis, full employment is a matter of political will — a matter of the determination of governments to pursue policies which create rather than destroy jobs by utilizing the enormous potential we have for growth at the community and national levels. The example of Saskatchewan demonstrates how greater democratic control of our economy can produce greater stability in employment and new job opportunities. I think it also has to be stressed that full employment is the first line of defence for our social security system, and that spending to create jobs is vastly more efficient than welfare programs which enforce dependency and breed despair. I would add that full employment is — or should be — a moral priority for Canadians.

Our Action Group concluded that new expenditures on community initiatives and badly needed new services — such as a national child care system — could quite feasibly reduce unemployment by at least 2.5 per cent per year, with every little increase in the government deficit. Elimination of unproductive corporate tax breaks and the like would be sufficient to pay for these initiatives. It is really just a matter of our determination to act.

There is a great fear of large deficits in this country. Unfortunately, when governments are afraid of deficits, they clamp down on the people who are the easiest to attack, they cut back on programs that benefit the poorest in our country. Whether it is an attempt to de-index old age pensions or family allowances, freeze minimum wages, or cut back social programs, the poor are

the ones who suffer most. On the other hand, the government is very quick to hand out millions of dollars to big banks, or subsidize the takeover of Gulf Oil, though these actions create very few jobs. Again, it is a matter of choice.

My closing remarks concern free trade with the United States. I am in favour of multilateral reduction of tariff and non-tariff barriers, but I am concerned that bilateral free trade with the United States could cost many jobs in this country and dangerously compromise our capacity to pursue policies which would lead us to full employment.

Canada has developed a large number of institutions that supplant the role of the market in our economic life. Marketing boards would be one example, the CBC another. What is really at stake is our capacity to plan our own future — for the U.S. objects to these non-market mechanisms which are, in their view, obstacles to free trade.

I would argue that we need a vision that is larger and broader than the idea of locking Canada into Fortress America, a vision of a more self-reliant Canada committed to the goal of full employment and willing to democratize economic decision making to that end.

Full employment is ultimately a matter of choice and will. We have the capacity and the potential at the community and the national levels to provide useful and productive work for all. What is lacking is the vision and the determination to turn potential into reality.

The Canadian Council on Social Development

Founded in 1920, the Canadian Council on Social Development (CCSD) is an independent, national, non-profit organization. Through research, policy analysis, community consultation and information sharing, the CCSD provides a forum for citizen participation in the formulation of progressive social policies.

The CCSD is the only national organization whose mandate and involvement embrace all aspects of social development and social policy. Since its beginning, the Council has been actively involved in the evaluation of existing programs, the identification of essential improvements, and the promotion of needed developments. It has been a positive, non-partisan advocate of social measures such as universal inoculation, pensions, unemployment assistance, workmen's compensation, medicare, legal aid, daycare, and social and cooperative housing. The Council played an active role in the development of the Canada Assistance Plan and the Child Tax Credit, and has been a promoter of the Guaranteed Annual Income concept.

The CCSD is not a "think tank." It is the only national social research, advocacy and policy organization with an open public membership. CCSD's analyses, opinions, research and information reflect not only highly professional technical work but also the active analysis and shared experience of its broadly representative membership.

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The CCSD is a major publisher in the social development field. Periodical publications include *Perception*, a bilingual magazine of social analysis, and three quarterly newsletters: *Initiative* (self-help), *Vis-à-vis* family violence), and *Overview* (social development issues).

CANADIAN COUNCIL ON SOCIAL DEVELOPMENT

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This is a book that will interest all people concerned with Canada's economic and social choices.

The Editors

Duncan Cameron is a political economist at the University of Ottawa. He is the co-author of *Ethics and Economics* (with Gregory Baum), co-editor of *The Other Macdonald Report* (with Daniel Drache) and *Canada and the New International Division of Labour* (with François Houle), and editor of *Explorations in Canadian Economic History* and *The Free Trade Papers*.

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Canadian Council on Social Development
ISBN 0-88810-377-8 (paper)
ISBN 0-88810-381-6 (hardcover)